Supreme Court, U.S.
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No. 00-

In the Supreme Court of the United States

CUSTOM FOOD MACHINERY, INC. and RON MCNIEL, SR.,

Petitioners,

v.

MARIA TERESA DE SARACHO, EUREKA CANNERS GROUP, S.A. and EUREKA MEXICANA, S.A.,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Judgment in the amount of $12.5 million was entered on a jury verdict against petitioners, an individual and his privately owned corporation. The amount of the verdict was based on testimony by an accounting expert that was indisputably wrong and resulted in an undeniable $6 million windfall to the plaintiffs. The United States Court of Appeals for the Ninth Circuit upheld the district court's admission of this testimony under Rule 703 of the Federal Rules of Evidence over petitioners' objection to its lack of reliability. In conflict with the decisions of other circuit court of appeals that have considered the issue since this Court's decision in *Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579 (1993), the Ninth Circuit ruled that for purposes of admissibility, it was enough that the accountant, in forming his opinion, had relied on information of a type on which accountants customarily rely. Thus, the following question is presented:

> Whether a challenge to the reliability of the bases for an expert opinion under Rule 703 requires not only that the proponent of the evidence satisfy the court that the facts, data or opinions considered by the expert are of the type customarily relied upon by experts in the field but also that such items are sufficiently trustworthy to make such reliance reasonable in the particular case.

LIST OF PARTIES AND CORPORATE DISCLOSURE STATEMENT

Petitioners Custom Food Machinery, Inc. and Ron McNiel, Sr. were defendants and appellants in the courts below. Respondents Maria Teresa De Saracho, Eureka Canners Group, S.A. and Eureka Mexicana, S.A. were plaintiffs and appellees. Fred Avalli was a defendant and appellant in the courts below.

Pursuant to Supreme Court Rule 29.6, petitioner Custom Food Machinery, Inc. states that it has no parent corporation and that no publicly held company owns 10% or more of its stock.

TABLE OF CONTENTS

Page

QUESTION PRESENTED i

LIST OF PARTIES AND CORPORATE DISCLOSURE STATEMENT ii

OPINIONS BELOW 1

JURISDICTION 1

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED 1

STATEMENT OF THE CASE 2

REASONS FOR GRANTING THE PETITION 4

I. Certiorari Should Be Granted to Resolve the Split in the Circuits Regarding the Court's Duty to Determine Whether the Particular Data on Which the Expert Relies are Reliable. 6

II. The Ninth Circuit's Decision Is an Abdication of the Court's Gatekeeping Function and Has Produced a Serious Miscarriage of Justice. 14

CONCLUSION 15

TABLE OF AUTHORITIES

Page(s)

Cases:

Bradley v. Armstrong Rubber Co., 130 F.3d 168 (5th Cir. 1997) 4

Daubert v. Merrell Dow Pharmaceuticals, Inc. 509 U.S. 579 (1993) ..... passim

Frye v. United States, 293 F. 1013 (D.C. Cir. 1923) 11

Gong v. Hirsch, 913 F.2d 1269 (7th Cir. 1990) 9

Guillory v. Domtar Industries Inc., 95 F.3d 1320 (5th Cir. 1996) 8, 14

Head v. Lithonia Corp., 881 F.2d 941 (10th Cir. 1989) 9

In re "Agent Orange" Product Liability Litigation, 611 F. Supp. 1223 (E.D.N.Y. 1985), *aff'd*, 818 F.2d 187 (2d Cir. 1987) 7

In re Japanese Electronic Products Antitrust Litigation, 723 F.2d 238 (3d Cir.1983), *rev'd on other grounds*, 475 U.S. 574 (1986) 12

In re Paoli Railroad Yard PCB Litigation, 35 F.3d 717 (3d. Cir. 1994), *cert. denied*, 513 U.S. 1190 (1995) 7, 10, 12

In re TMI Litigation, 193 F.3d 613 (3d Cir. 1999), *cert. denied*, 120 S.Ct. 2238 (2000) 8

Manniano v. Int'l Mfg., 650 F.2d 846 (6th Cir. 1981) 10

Mapco, Inc. v. Carter, 573 F.2d 1268 (TECA), *cert. denied*, 437 U.S. 904 (1978) 10

Renaud v. Martin Marietta Corp., 972 F.2d 304 (10th Cir. 1992) 9

TABLE OF AUTHORITIES (continued)

Page(s)

Sementilli v. Trinidad Corp., 155 F.3d 1130 (9th Cir. 1998) 11

Shaw by Strain v. Strackhouse, 920 F.2d 1135 (3d Cir. 1990) 14

Slaughter v. Southern Talc Co., 919 F.2d 304 (5th Cir. 1990) 8

Trepel v. Roadway Express, 194 F.3d 708 (6th Cir. 1999) 10

United States v. City of Miami, 115 F.3d 870 (11th Cir. 1997) 4, 8

United States v. Corey, 207 F.3d 84 (1st Cir. 2000) 9

United States v. Locascio, 6 F.3d 924 (2d Cir. 1994), *cert. denied*, 511 U.S 1070 (1994) 8

Washington v. Armstrong World Industries, Inc., 839 F.2d 1121 (5th Cir. 1988) 10

Statutes and Codes:

Title 28, United States Code
Section 1257(a) 1
Section 1332 2

Rules:

Federal Rules of Evidence
Rule 104(a) 11, 13
Rule 702 ..... 5, 12
Rule 703 ..... passim

TABLE OF AUTHORITIES (continued)

Page(s)

Other Authorities:

2 M. H. Graham, *Handbook of Federal Evidence*, § 703.1 (4th ed. 1996) 6, 10, 13

3 Mueller & Kirkpatrick, *Federal Evidence* § 357 (2d ed. 1994) 13

Advisory Committee Notes, Rule 803 (1972 Proposed Rules) 6

Epps, *Clarifying the Meaning of Federal Rule of Evidence 703*, 36 B.C. L. Rev. 53 (1994) 6, 12

Imwinkelried, *Developing a Coherent Theory of the Structure of Federal Rule of Evidence 703*, 47 Mercer F. Rev. 477 (1996) 13

PETITION FOR A WRIT OF CERTIORARI

Custom Food Machinery, Inc. and Ron McNiel, Sr. respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Ninth Circuit.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Ninth Circuit (App. 1a-13a) is reported at 206 F.3d 874 (9 Cir. 2000). The relevant opinion and orders of the United States District Court for the Northern District of California (App. 14a-21a) are unreported.

JURISDICTION

The Ninth Circuit's final judgment was entered on March 3, 2000. The petition for rehearing timely filed by petitioners was denied on April 17, 2000. App. 22a. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

Rule 703 of the Federal Rules of Evidence provides as follows:

> The facts or data in the particular case on which an expert bases an opinion or inference may be those perceived by or made known to the expert at or before the hearing. If of a type reasonably relied upon by experts in the particular field in forming opinions or inferences upon the subject, the facts or data need not be admissible in evidence.

STATEMENT OF THE CASE

This is an action brought by a Mexican company, Eureka Canners Croup, S.A. ("ECG"), and two of its minority shareholders, Maria Teresa De Saracho ("Maria") and her family's corporation Eureka Mexicana, S.A. ("Mexicana"). Reporter's Transcript ("RT") 358-59, 377-79, 915-17. Maria and her husband Cesar De Saracho formed ECG with defendant Fred Avalli ("Avalli") in August 1993 for the purpose of starting a tomato canning and processing plant in Culiacan, Sinaloa, Mexico. RT 332-34. Petitioner Custom Food Machinery, Inc. ("CFM") sold ECG food processing equipment to be used at the plant.

Plaintiffs filed this diversity action (28 U.S.C. § 1332) against Avalli and petitioners in 1995 alleging claims for fraud, conspiracy to defraud and breach of fiduciary duty. Plaintiffs alleged that they had been defrauded in two principal respects: (1) that they were led to believe that Avalli had made a $1,050,000 capital contribution to ECG that Avalli never made; and (2) that they were led to believe ECG was purchasing from CFM fully guaranteed food processing equipment worth $2.15 million, when in fact ECG paid only $1.1 million for equipment sold "as-is" and without warranty.

As a result of this alleged fraud, plaintiffs claimed that ECG's canning business collapsed, causing ECG to default on loans to a Mexican bank (BanRural). Plaintiffs themselves claimed not to know how much they owed BanRural, but their expert Stephen Degnan testified, over objection, that ECG's liability on the BanRural loans was nearly $11.4 million at the time of trial. RT 1705.[1] In closing argument, plaintiffs' counsel asked the jury to award approximately $15.7 million in

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[1] At trial, the defendants objected contemporaneously to the proffered expert testimony and also made a motion to strike after its erroneous admission. App. 16a-21a.

damages to plaintiffs--$11.4 million for plaintiffs' alleged liability to BanRural and $4.3 million for lost profits and other damages. RT 3275-79. The jury returned a verdict against petitioners for $12,516,000. App. 14a-15a.[2]

Thus, the judgment was necessarily based on the expert testimony concerning the BanRural loans, which comprised plaintiffs' major element of damages. Their expert arrived at his $11.4 million figure by taking the amount due on ECG's three loans as of April 7, 1995 (as shown on notices of default issued by BanRural) and adding purported "default" interest to those amounts to bring them current through the time of trial. RT 1704; ER 1511, 1558-77. The expert testified, based on the written loan agreements between the bank and ECG, that the appropriate "default" interest rate was 1.5 times the higher of two peso reference rates--BanRural's costs of funds and the Mexican T-bill rate. ER 1511; RT 1695, 1697-1703. Using this methodology, plaintiffs' expert opined that the bank charged post-defaults rates of interest ranging from 41-90%. RT 1702-03. The highest interest rate computed—90.59%—was for the second quarter of 1995 beginning on April 8. RT 1704.

In fact, the expert's testimony was wildly inaccurate, having been based on assumptions as to the applicable interest rate that were indisputably wrong and inconsistent with BanRural's actual practices. Rather than the expert's super-usurious rates, the bank itself claimed post-default interest as of April 7, 1995 at rates of only 23.7% and 22.5% on two of the loans. ER 1564, 1572. Interest on the third loan on that date was charged at the non-default rate of 13.5%. ER 1558. Moreover,

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[2] Judgment likewise was entered against Avalli for $12,516,000. *Id.* The jury also found that Avalli had acted with oppression, fraud or malice, but that petitioners had not. Excerpts of Record ("ER") 191.

in post-judgment motions, petitioners presented BanRural's response to letters rogatory and an affidavit by the responsible bank officer attesting that, as of six months after trial, the amount of the debt was less than $5.5 million. See ER 280:10-12, 281:22-28, 416, 483, 1242-46. Thus, the judgment represents an undeniable windfall to plaintiffs of $6 million.

On appeal to the Ninth Circuit, petitioners argued that, pursuant to Rule 703 of the Federal Rules of Evidence, the district court should have sustained their objection and motion to strike the expert's testimony on the ground that its unreliability violated basic rules of admissibility. In a 2-to-1 decision, the court of appeals rejected petitioners' challenge to admission of the erroneous expert testimony.

The panel opinion invoked Rule 703 and approved of the expert's reliance on the loan agreements to generate his erroneous testimony. The court evaluated admissibility solely on the basis of custom in the field of accountancy: "[i]t is common sense that certified public accountants reasonably rely on loan agreements to calculate the interest due on loans." App. 8a. The dissent recognized, however, that it was manifestly erroneous for the district court to overrule defendants' objection, reasoning that "[e]xpert testimony based on incorrect underlying facts should be excluded" (citing *United States v. City of Miami*, 115 F.3d 870, 873 (11th Cir. 1997) and *Bradley v. Armstrong Rubber Co.*, 130 F.3d 168, 177 (5th Cir. 1997)). App. 13a.

REASONS FOR GRANTING THE PETITION

Certiorari should be granted to resolve a pervasive conflict in the circuit courts of appeals regarding the standard for admission of expert testimony under Rule 703 of the Federal Rules of Evidence. The Court has yet to address this important question. Until it does, resolution of the issue—on which the outcome in many

cases hinges—will depend on the circuit in which the action is filed.

The question presented in this case involves the Rule 703 standard that should apply to the underlying data on which expert opinion testimony is based. The majority of courts considering this issue have held that the test for admission of opinion evidence is two-pronged. First, the proponent must present evidence that the opinion is based on the general types of underlying facts, information or data on which experts in the field customarily rely. Second, the district court must be satisfied that the particular information supporting the opinion is sufficiently reliable to permit admission of the expert's testimony. Most of the recent decisions following the majority approach have relied on the Court's reasoning in *Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579 (1993).[3]

Because *Daubert* does not dispose of the issue presented under Rule 703, some circuit courts of appeals, including the Ninth Circuit below, continue to follow a less stringent approach to the admission of opinion testimony under Rule 703. According to the minority approach followed by the Sixth and Ninth Circuits, expert testimony is admissible under Rule 703 so long as the foundational data for the expert's opinion are of the general sort on which other experts customarily rely. Thus, as in this case, expert testimony is admitted without any inquiry into the reliability of the actual underlying information on which the opinion is based.

Scholarly authorities have recognized the split in the circuits and support adoption of the more restrictive

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[3] *Daubert* involved a related question arising under Rule 702: whether expert opinion based on scientific technique is inadmissible unless the technique is "generally accepted" as reliable within the relevant scientific community.

approach. *See, e.g.*, Epps, *Clarifying the Meaning of Federal Rule of Evidence 703*, 36 B.C. L. Rev. 53, 75-76 (1994). This conclusion is based, at least in part, on the recognition that the competing liberal approach to evaluation of the foundation for expert testimony is unprincipled, transfers control of the admissibility of evidence to the expert and creates the potential for errors in the adjudicative process. *See id.* at 77. It also is inconsistent with the overriding concept of the Federal Rules of Evidence that, to be admissible, evidence must possess sufficient circumstantial guarantees of trustworthiness and reliability. *See generally* Advisory Committee Notes, Rule 803 (1972 Proposed Rules); 2 M. H. Graham, *Handbook of Federal Evidence*, § 703.1, pp. 103-09 & n.17 (4th ed. 1996).

This case presents a stark illustration. The Ninth Circuit upheld admission of the opinion of plaintiffs' expert that, based on the application of super-usurious interest rates supposedly dictated by loan document formulae, the amount due on the BanRural loans had mushroomed at the time of trial to nearly $11.4 million. The district court admitted this testimony despite the evidence in the record reflecting that the bank itself had not charged interest at the rates that formed the basis for the expert's opinion. Contrary to the Ninth Circuit's conclusion (App. at 8a-9a, fn. 5), such expert testimony could not create a factual issue for the jury. This Court should grant certiorari and rule that the district judge should have excluded the opinion under Rule 703 and remand the case for a new trial.

I. Certiorari Should Be Granted to Resolve the Split in the Circuits Regarding the Court's Duty to Determine Whether the Particular Data on Which the Expert Relies are Reliable.

The circuits are divided over whether Federal Rule of Evidence 703 requires a trial judge to assess independently the reliability of the bases of an expert

opinion. *See, e.g., In re "Agent Orange" Product Liability Litigation*, 611 F. Supp. 1223, 1243-44 (E.D.N.Y. 1985), *aff'd*, 818 F.2d 187 (2d Cir. 1987) (describing the two approaches: "The more restrictive view requires the trial court to determine not only whether the underlying data are reasonably relied upon by experts in the field, but also whether the underlying data are untrustworthy for hearsay or other reasons. The more liberal view ... allows the expert to base an opinion on data of the type reasonably relied upon by experts in the field without separately determining the trustworthiness of the particular data involved." (citations omitted)). The Second, Third, Fourth, Fifth, Seventh, Tenth, and Eleventh Circuits apply the more rigorous restrictive approach, while the Sixth and Ninth Circuits apply the unprincipled, liberal approach.

Under the restrictive approach to Rule 703, courts require not only that the underlying facts, opinions or data be of a type on which experts in the field customarily rely, but also that such items be sufficiently trustworthy to make such reliance reasonable in a particular case. This two-step approach is best illustrated by the Third Circuit's opinion *In re Paoli Railroad Yard PCB Litigation*, 35 F.3d 717 (3d. Cir. 1994), *cert. denied*, 513 U.S. 1190 (1995). The Third Circuit ruled that the admissibility of expert testimony under Rule 703 cannot rest on a finding merely that the expert's opinion conforms to accepted standards within the relevant field:

> [w]e now make it clear that it is the judge who makes the determination of reasonable reliance, and that for the judge to make the factual determination under Rule 104(a) that an expert is basing his or her opinion on a type of data reasonably relied upon by experts, the judge must conduct an independent evaluation into reasonableness. . . . [T]here must be good grounds on which to find the data reliable.

Id. at 748; *see also In re TMI Litigation*, 193 F.3d 613, 697 (3d Cir. 1999), *cert. denied*, 120 S.Ct. 2238 (2000) ("If the data underlying the expert's opinion are so unreliable that no reasonable expert could base an opinion on them, the opinion resting on that data must be excluded. The key inquiry is reasonable reliance and that inquiry dictates that the trial judge must conduct an independent evaluation into reasonableness. . . . [T]here must be good grounds on which to find the data reliable."(citations omitted)). Likewise applying the restrictive approach, the Fifth Circuit has held that "though the district court serves as a gatekeeper for expert evidence, it is an important role designed to extract evidence tainted by farce or fiction. Expert evidence based on a fictitious set of facts is just as unreliable as evidence based upon no research at all." *Guillory v. Domtar Industries Inc.*, 95 F.3d 1320, 1331 (5th Cir. 1996); *see also Slaughter v. Southern Talc Co.*, 919 F.2d 304, 306-07 (5th Cir. 1990) (finding that despite the fact that the expert's methods were widely accepted in the medical community, Rule 703 "requires courts to examine the reliability of an expert's sources to determine whether they satisfy the threshold established by the rule").

Other circuits also have announced the requirement that district courts must conduct independent review of the trustworthiness of an expert's particular bases for opinion before admitting it. *See, e.g., United States v. City of Miami*, 115 F.3d at 873-74 (observing that "opinions derived from erroneous data are appropriately excluded" and finding that the lower court erred in adopting expert testimony that "did not examine legally relevant factors and was derived from erroneous data"); *United States v. Locascio,* 6 F.3d 924, 938 (2d Cir.), *cert. denied*, 511 U.S 1070 (1994) (stating that the trial court is "not bound to accept expert testimony based on questionable data simply because other experts use such data in the field"); *Renaud v. Martin Marietta Corp.*, 972 F.2d 304, 308 (10th Cir. 1992) (finding that the

district court "had an independent duty . . . to decide whether the single data point supported the admissibility of the conclusions [the experts] sought to draw therefrom . . . [and that] pursuant to the Fed.R.Evid. 703, the District Court has the responsibility of evaluating the trustworthiness of the factual basis upon which an expert witness relies"); *Gong v. Hirsch*, 913 F.2d 1269, 1272-73 (7th Cir. 1990) (concluding that despite finding that observations by staff personnel were a type of information reasonably relied upon by experts in the field, obvious concerns about lack of trustworthiness of the particular data were sufficient to have warranted exclusion of the opinion testimony); *Head v. Lithonia Corp.*, 881 F.2d 941, 943 (10th Cir. 1989) ("The limitation that the facts and data be the type reasonably relied upon by experts in the field provides a mechanism by which the court can evaluate the trustworthiness of the underlying data on which the expert relies." (citations omitted)).[4]

In sharp contrast to these decisions applying the more restrictive standard, the Ninth Circuit in this case approved of the district court's failure to make an independent assessment of the trustworthiness of the data on which the expert relied (and, hence, the reasonableness of such reliance). In response to petitioners' challenge to the lack of reliability of those underlying data, the majority opinion below stated that "[i]t is common sense that certified public accountants reasonably rely on loan agreements to calculate the interest due on loans." App. 8a. Thus, according to the Ninth Circuit, the district court had no obligation to determine whether the expert's reliance on the loan

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[4] *Cf. United States v. Corey*, 207 F.3d 84, 89 (1st Cir. 2000) (stating that "Rule 703 does require that the trial judge act as an independent 'gatekeeper' to ensure that there is sufficient, credible evidence that experts do rely on the specified types of sources in formulating their opinions").

agreements was reasonable under the circumstances of this case. Instead, the appellate court erroneously concluded that this simply presented a jury issue. App. 8a-9a, fn. 5.[5] As a result, the court approved of the admission of highly prejudicial evidence as to the amount of the BanRural indebtedness—opinion testimony that was indisputably incorrect.

Characterized by an unyielding faith in the expert, the Ninth Circuit's liberal approach leaves questions about the reliability of the evidence to the cross-examination skills of opposing counsel and the absolute wisdom of the jury. Joining the Ninth Circuit, the Sixth Circuit also applies the liberal approach, stating "[g]reat liberality is allowed the expert in determining the basis of his opinion under Rule 703." *Manniano v. Int'l Mfg.*, 650 F.2d 846, 853 (6th Cir. 1981). The more restrictive two-step assessment of expert evidence has gained acceptance in the Sixth and Ninth Circuits only in dissenting opinions. *See, e.g., Trepel v. Roadway Express*, 194 F.3d 708, 722 (6th Cir. 1999) (Suhrheinrich, J., dissenting in part) ("By

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[5] Judicial and scholarly authorities are unanimous that the admission of expert opinion testimony under Rule 703 presents a preliminary question for the court to determine pursuant to Rule 104(a). *See, e.g., In re Paoli*, 35 F.3d at 748; *see also* 2 M. H. Graham, *supra*, § 703.1, p. 103. Moreover, no reasonable juror in this case could have concluded that, as plaintiffs' expert opined, the bank was actually demanding more interest than what its contemporaneous documents said it was demanding. The notices stating the interest rate that BanRural was actually assessing were undisputed and indisputable, and demonstrably erroneous expert testimony cannot create a factual conflict. *E.g., Washington v. Armstrong World Industries, Inc.*, 839 F.2d 1121, 1123 (5th Cir. 1988) (inadmissible expert affidavit cannot raise genuine issue of material fact to defeat summary judgment motion); *Mapco, Inc. v. Carter*, 573 F.2d 1268, 1282 (Temp. Emer. Ct. App.), *cert. denied*, 437 U.S. 904 (1978) (same).

ensuring that an expert's opinion is based on reliable information, the courts prevent the abuse of expert testimony by those who seek to use experts as a pretense for the admission of otherwise inadmissible and unreliable hearsay."); *Sementilli v. Trinidad Corp.*, 155 F.3d 1130 (9th Cir. 1998) (B. Fletcher, J., dissenting) (noting that the Supreme Court's holding in *Daubert* stressed that "in ruling on admissibility, trial judges are the gatekeepers and should pay particular attention to the reliability of the expert and his or her testimony" (citations omitted)).

The restrictive approach is consistent with this Court's reasoning in *Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579 (1993). In *Daubert*, the Court considered whether scientific expert testimony, to be admissible under Rule 702, has to be based on scientific techniques "generally accepted" by experts within the field. The Court answered this question in the negative, ruling that the "uncompromising 'general acceptance' test" first developed in *Frye v. United States*, 293 F. 1013, 1014 (D.C.Cir. 1923), was not the touchstone under Rule 702. 509 U.S. at 596. Rather, the Court held in *Daubert* that scientific opinion testimony is admissible as long as the trial judge makes a preliminary determination, in accordance with Rule 104(a), that the proffered testimony (1) has sufficient indicia of scientific validity and reliability and (2) will assist the trier of fact to understand or determine a fact in issue. *Id.* at 592-95.

Daubert also emphasized the critical role of the trial judge in controlling the admission of expert testimony under the Federal Rules of Evidence. 509 U.S. at 589-90. The "gatekeeping role for the judge" (*id.* at 597), for example, was this Court's answer in *Daubert* to the argument that abandonment of "general acceptance" as the exclusive requirement for admission of scientific opinions would "result in a 'free-for-all' in which befuddled juries are confounded by absurd and irrational

pseudoscientific assertions." *Id.* at 595. In reliance on this language in *Daubert*, the Third Circuit in *In re Paoli*, 35 F.3d at 748, disavowed its adherence to the liberal approach to the admissibility of expert testimony under Rule 703, overruling its holding in *In re Japanese Electronic Products Antitrust Litigation*, 723 F.2d 238, 276 (3d Cir.1983), *rev'd on other grounds*, 475 U.S. 574 (1986).[6]

Daubert, however, does not resolve the conflict in the circuits as to the proper test under Rule 703. Although in *Daubert* this Court did offer "some general observations" about the district court's gatekeeping role (509 U.S. at 593), it did not endorse the restrictive approach adopted by the majority of courts and did not decide the question of the admissibility of expert opinion testimony under Rule 703 based on the nature of the underlying, facts, data and information supporting the opinion. Thus, even after of *Daubert*, the Ninth Circuit in this case failed to impose any duty on the trial judge to make a preliminary assessment of the trustworthiness of the particular data on which the expert relied. Certiorari therefore should be granted to give needed guidance on an important issue having broad practical implications in virtually all trials conducted in federal courts.

Academic authority has recognized the conflict between the circuits and the need for uniformity and has encouraged adoption of the restrictive approach. *See, e.g.*, Epps, *supra*, 36 B.C. L. Rev. at 84 ("Rule 703 has been misunderstood and misapplied during it's twenty

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[6] Whereas in *In re Japanese Products*, the Third Circuit had stated that under Rule 703, "[t]he proper inquiry is not what the court deems reliable, but what the experts in the relevant discipline deem it to be" (723 F.2d. at 276), the court now has concluded that after *Daubert*, the judge's role as gatekeeper is to determine whether the data underlying an expert opinion are reliable. *See In re Paoli*, 35 F.3d at 748.

year history."); Imwinkelried, *Developing a Coherent Theory of the Structure of Federal Rule of Evidence 703*, 47 Mercer F. Rev. 477, 464 (1996) (calling for courts to effectively resolve the splits in authority by defining the scope of Rule 703). The academic world has largely taken the position that the restrictive approach is properly applied. *See, e.g.*, 2 M. H. Graham, *supra,* § 703.1, p. 105, fn. 14 ("The proper role of the trial judge in determining whether reliance is reasonable is still subject to occasional dispute although the so-called restrictive approach correctly clearly dominates."); 3 Mueller & Kirkpatrick, *Federal Evidence* § 357 (2d ed. 1994) (recognizing the dual standard yet noting that it is "inconceivable that the courts should defer completely to experts"). Indeed, as articulated by one of the leading commentators, Rule 703 mandates application of the more stringent, two-pronged test:

> [T]he proponent of the evidence must satisfy the court, both that . . . [the facts, data or opinions] are of the type customarily relied upon by experts in the field and that such items are sufficiently trustworthy to make such reliance reasonable.

2 M. H. Graham, *supra*, § 703.1, p. 105 (footnotes omitted).

For the expert testimony here to be admissible over petitioners' objection to its reliability, it was not enough that certified public accountants customarily rely on loan documents in determining the amount of interest due on loans. Rather, it was also necessary that those sources of information were sufficiently reliable here to make the expert's reliance on them reasonable.

II. The Ninth Circuit's Decision Is an Abdication of the Court's Gatekeeping Function and Has Produced a Serious Miscarriage of Justice.

Plaintiffs did not seriously contend below that ECG actually owed BanRural $11,395,000 in May 1997, as their expert testified. To the contrary, the expert's assumptions as to the interest rates effective in April 1995 were undeniably incorrect and directly refuted by the record evidence (i.e., the interest rates actually charged by the bank at that time). Therefore, as the dissent recognized (App. 12a-13a), it was manifestly erroneous for the district court to overrule defendants' objection. *See, e.g., Guillory v. Domtar Industries, Inc.*, 95 F.3d at 1331 ("[N]othing in Rule 703 requires a court to admit an [expert] opinion based on facts that are indisputably wrong."); *Shaw by Strain v. Strackhouse*, 920 F.2d 1135, 1142 (3d Cir. 1990) (trial court properly disregarded expert's conclusion that rested on assumption shown contrary to facts of record).

Had the Ninth Circuit followed the correct, more restrictive approach, it would have reached the correct result and excluded the fanciful opinion offered by plaintiffs' accounting expert. As to the first prong of the test, the majority opinion below is correct (App. at 8a): loan documents are among the general types of information on which accountants rely to determine the amount of interest due on loans. The underlying data supporting the opinion, however, did not meet the second component of the test for admissibility under Rule 703. The record reflects the dramatic and unexplained disparity between the expert's interest rate assumptions based on the loan documents and the evidence reflecting the bank's actual practices with respect to computing interest. As a result, the district court should have sustained petitioners' objection to the lack of reliability of the data underlying the expert's opinion, and the court of appeals should have reversed

the trial judge's failure to exclude this highly prejudicial testimony.

This result is consistent with *Daubert* and proper as a matter of policy. The trial judge should have exercised a gatekeeping role under Rule 703 to evaluate the reasonableness and reliability of the data on which plaintiffs' expert relied. This is what is envisioned by *Daubert* and mandated by the majority of the court of appeals decisions, which apply the proper approach. The expert's testimony was indisputably wrong and its exclusion would have avoided an undeniable $6 million windfall. Under Rule 703, trial courts must refuse to admit expert testimony, such as that proffered below, that is premised on underlying data and information that lack sufficient guarantees of reliability and trustworthiness. It is not proper to leave it up to the expert or the jury to sort through such preliminary issues. Until this Court addresses the issue, however, the lower courts will be free to follow the liberal, unprincipled approach, which creates the potential for irrational results of the type that occurred here.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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APPENDIX A

UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

Maria Teresa DE SARACHO, Eureka Canners Group, S.A., a corporation formed under the laws of Mexico; Eureka Mexicana SA, a corporation formed under the law of Mexico, Plaintiffs-Appellees,

v.

CUSTOM FOOD MACHINERY, INC., a California corporation; Ron McNeil, Sr., Defendants-Appellants, and Fred Avalli, and Doe 1 through Doe 25, inclusive, Defendant-Appellant.

Nos. 98-15003, 98-15007 and 98-17051.

Argued and Submitted Dec. 8, 1999.

Submission Vacated Dec. 15, 1999.

Resubmitted Jan. 27, 2000.

Decided March 3, 2000.

Thomas V. Loran, III, Pillsbury, Madison & Sutro, San Francisco, California, for the defendants-appellants.

William J. Keegan, The Keegan Law Group, San Jose, California, for the plaintiffs-appellees.

Appeals from the United States District Court for the Northern District of California; William A. Ingram, District Judge, Presiding. D.C. No. CV-95- 20854-WAI.

Before: BRIGHT,[1] PREGERSON and W. FLETCHER, Circuit Judges.

Opinion by Judge PREGERSON; Dissent by Judge BRIGHT.

PREGERSON, Circuit Judge:

This appeal requires us to review four procedural decisions made by the district court before, during, and after a jury trial that resulted in a $12.5 million verdict against defendants. Defendants contend that the district court erred in denying (1) a motion *in limine* seeking dismissal of one plaintiff; (2) a motion to strike expert testimony; (3) a motion for a new trial; and (4) a motion for relief from judgment. We have jurisdiction under 28 U.S.C. § 1291, and we affirm the district court's denial of all four motions.

I

Plaintiffs in this suit are Eureka Canners Group, S.A. ("ECG"), Maria De Saracho, and Eureka Mexicana, S.A. ("Mexicana"). Defendants are Custom Food Machinery, Inc. ("Custom"), Fred Avalli ("Avalli"), and Ron McNeil, Sr. ("McNeil"). ECG is a Mexican corporation that was formed in 1993 by Maria De Saracho, Mexicana's owner Cesar De Saracho, and Avalli to process and can tomatoes in Sinaloa, Mexico. Custom is a California corporation that sold food processing equipment to ECG. McNeil is Custom's president and controlling shareholder.

Shortly after its formation, ECG took out three loans from Banco de Credito Rural del Pacifico Norte, S.N.C. ("BanRural"), a Mexican bank, totaling more than $3.3 million. Maria De Saracho guaranteed the BanRural loans, executed promissory notes on the loans, and pledged her property as collateral. In May 1995, BanRural declared ECG's loans in default. The following month, ECG filed a

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[1] The Honorable Myron Bright, Circuit Judge for the Eight Circuit Court of Appeals, sitting by designation.

lawsuit against BanRural in Mexican court, seeking to invalidate the trust agreement between Maria De Saracho and BanRural and to release the assets pledged as collateral for the loans. Later that year, BanRural filed an action against ECG in Mexican court ("BanRural litigation" or "BanRural suit"), seeking court orders designating an appraiser to value the assets pledged to the trust and allowing BanRural's representatives to enter ECG property to value its assets. BanRural did not seek a money judgment against ECG or Maria De Saracho. In March 1997, the Mexican court ruled that BanRural's representative lacked authority to sue in BanRural's name. In May 1998, a Mexican appeals court reversed that ruling.

Plaintiffs filed this lawsuit in December 1995, asserting claims for fraud, conspiracy to defraud, and breach of fiduciary duty. The case was tried before a jury during June and July 1997. At trial, plaintiffs attempted to prove that (1) defendants misrepresented that Avalli made a capital contribution to ECG of $1,050,000; (2) Maria De Saracho guaranteed the BanRural loans in reliance on that representation; (3) defendants misrepresented the value and quality of tomato processing equipment sold by Custom to ECG, causing the tomato processing business to fail; and (4) Custom paid kick-backs to Avalli. Plaintiffs sought damages for liability on the amount due on the BanRural loans in the sum of $11,395,457; ECG's lost profits which plaintiffs' expert testified exceeded $15,000,000; consequential damages; emotional distress; and reputational injury.

To prove the amount ECG owed to BanRural on the defaulted loans, plaintiffs introduced into evidence the loan agreements and promissory notes. Plaintiffs also presented two expert witnesses. Stephan Degnan, a certified public accountant, testified that the interest rate provisions in the loan documents required ECG to pay a default interest rate that was 1.5 times greater than the higher of the Mexican T-Bill rate or BanRural's cost of funds. Based on those provisions, Degnan calculated that $11,395,457 was owed to BanRural. An expert in Mexican law testified that BanRural had a viable cause of action under Mexican law to collect on

the defaulted loans. Defendants did not present any evidence about the amount due on the loans or the viability of a foreclosure suit by BanRural. The jury awarded plaintiffs $12,516,000 in damages.

After the trial ended, defendants acquired new evidence purportedly proving that ECG owed significantly less than $11 million on the BanRural loans. According to defendants, Degnan mistakenly relied on the interest rate provision in the loan documents. They claim that as of February 1998, the sum of $5,447,553 was due on ECG's loans (instead of $11,395,457 as of May 1997).

II

ECG's Authorization to Bring Suit

Defendants argue that ECG was not properly authorized to sue defendants. Defendant Avalli first challenged ECG's authorization to sue in a motion *in limine* filed on May 6, 1997, over eight months after filing his answer. The district court denied the motion "without prejudice to its renewal after the introduction and consideration of evidence concerning who is and who is not party to the purported partnership agreement." Avalli raised the same issue again at the close of the plaintiffs' case in chief in a Rule 50(a) motion for judgment as a matter of law. The district court denied the motion because it was untimely and "should have been determined before this case came for trial."[2] After the jury rendered its verdict, Avalli renewed the motion for a judgment as a matter of law under Rule 50(b). The court also denied that motion because it was untimely. Defendants then appealed the judgment entered against them.

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[2] A reasonable interpretation of this ruling is that upon hearing the Rule 50(a) motion, the district court concluded that it should have denied defendants' motion *in limine* because defendant did not raise the authority to sue issue until the eve of trial.

We decline to review directly the district court's denial of the motion *in limine*.[3] An appellate court will not review a denial of summary judgment after there has been a trial on the merits and an adverse jury verdict. At that stage, the propriety of the district court's denial of the summary judgment motion is an "academic question." *See General Signal Corp. v. MCI Telecomms. Corp.*, 66 F.3d 1500, 1506 (9th Cir. 1995); *Lum v. City & County of Honolulu*, 963 F.2d 1167, 1169 (9th Cir. 1992); *Lama v. Borras*, 16 F.3d 473, 477 n.5 (1st Cir. 1994) (collecting cases). We see no reason to treat any differently the denial of defendants' motion *in limine* to dismiss for lack of authority to sue.[4]

Even if we were to review the denial of the motion *in limine* directly, we would agree with the district court that defendants waived any objection to plaintiff's authorization

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[3] Defendants do not appeal the district court's denial of their Rule 50(a) and (b) motions for judgment as a matter of law. In any event, the district court properly denied the Rule 50(b) motion because defendants did not make a Rule 50(a) motion at the close of all evidence. "[T]he requirement that the motion be made at the close of all evidence is to be strictly observed." *Patel v. Penman*, 103 F.3d 868, 878 (9th Cir. 1996) (quoting *Farley Transp. Co., Inc. v. Santa Fe Trail Transp. Co.*, 786 F.2d 1342, 1345 (9th Cir. 1986)). Moreover, this court may only review the denial of a Rule 50(a) motion under the stringent plain error standard. *See Kreines v. United States*, 959 F.2d 834, 836 (9th Cir. 1992); *Los Angeles Police Protective League v. Gates*, 907 F.2d 879, 883 (9th Cir. 1990).

[4] Defendants cast their authority to sue argument as a challenge to plaintiffs' standing to sue. Subject matter jurisdiction cannot be waived and may be raised at any time. *See United States v. Hays*, 515 U.S. 737, 742, 115 S.Ct. 2431, 132 L.Ed.2d 635 (1995). Even if defendants are correct that ECG lacked authorization to sue, this court does not lack subject matter jurisdiction in the sense that it would if plaintiffs lacked standing to sue under the "case or controversy" requirement of Article III of the Constitution. "The question of a litigant's capacity or right to sue or to be sued generally does not affect the subject matter jurisdiction of the district court." *Summers v. Interstate Tractor & Equip. Co.*, 466 F.2d 42, 50 (9th Cir. 1972).

to sue. A defendant must challenge a plaintiff's authority to sue by making a "specific negative averment." *See* FED. R. CIV. P. 9(a). Case law in this circuit states that the "specific negative averment" must be made "in the responsive pleading or by motion before pleading." *Summers v. Interstate Tractor & Equip. Co.*, 466 F.2d 42, 49-50 (9th Cir. 1972). Other authorities support this rule:

> [A]lthough an objection to a party's capacity is not an affirmative defense, it can be analogized to an affirmative defense and treated as waived if not asserted by motion or responsive pleading, subject, of course, to the liberal amendment policy of Rule 15. Early waiver is necessary to give meaning to the requirement in Rule 9(a) that capacity must be put in issue by a "specific negative averment."

5 Wright & Miller, FED. PRAC. & PROC. CIV. 2d § 1295; *see also Wagner Furniture Interiors, Inc. v. Kemner's Georgetown Manor, Inc.*, 929 F.2d 343, 345 (7th Cir.1991) (holding that averment was untimely because it was raised in a motion to dismiss at the final pre-trial conference); *MTO Maritime Transp. Overseas, Inc. v. McLendon Forwarding Co.*, 837 F.2d 215, 218 (5th Cir.1988) (finding that the capacity issue was waived because the defendant did not raise it "until the eve of trial in the Joint Pre-Trial Order").

Similarly, if the motion *in limine* is construed as a motion to amend the pleadings, the district court did not abuse its discretion in denying it as untimely. While "leave [to amend a pleading] shall be freely given when justice so requires," Fed.R.Civ.P. 15(a), a district court may deny the motion if it will cause unfair delay. *See Parker v. Joe Lujan Enterprises*, 848 F.2d 118, 121 (9th Cir. 1988); *McGlinchy v. Shell Chem. Co.*, 845 F.2d 802, 809 (9th Cir. 1988). "Where the party seeking amendment knows or should know of the facts upon which the proposed amendment is based but fails to include them in the original complaint, the motion to amend may be denied." *Jordan v. County of Los Angeles*, 669 F.2d 1311, 1324 (9th Cir.), *vacated on other grounds*, 459 U.S. 810, 103 S.Ct. 35, 74 L.Ed.2d 48 (1982), *on remand*, 713 F.2d 503

(9th Cir. 1983), *opinion amended,* 726 F.2d 1366 (9th Cir. 1984).

Defendants did not raise the authority to sue issue until one week before the trial was scheduled to begin. None of defendants made a "specific negative averment" in their answers, moved to amend their answers, or filed a motion for summary judgment on this issue. Nor was the authority to sue issue among the disputed factual issues listed in the Joint Pretrial Conference Statement filed with the court on April 21, 1997. Defendants seek to excuse their failure to raise the authority issue in a timely fashion by asserting that they obtained the relevant documents only two weeks prior to the *in limine* motion. Yet Avalli's counsel received the Partnership Agreement on February 28, 1997, but did not review it until May 7, 1997. According to defendants, the Partnership Agreement is the key document that establishes that Avalli's approval was necessary for ECG to bring suit. Moreover, defendants' attempt to shift blame to plaintiffs for not producing the documents earlier is unpersuasive because defendants never made a formal request for the documents under Rule 34.

III

Degnan's Opinion Testimony

Defendants argue that the district court erred in admitting opinion testimony by plaintiffs' expert Stephen Degnan regarding the amount ECG owed BanRural on the defaulted loans. At trial, defendants objected to Degnan's reliance on the BanRural loan agreements and promissory notes because they were not reliable. Defendants renewed the objection in a motion to strike. The district court denied the motion to strike, stating that "these documents have some indicia of reliability for what they purport to be."

We review a trial court's decision to admit or exclude expert testimony for an abuse of discretion. *Desrosiers v. Flight Int'l of Florida, Inc.*, 156 F.3d 952, 960 (9th Cir.), *cert denied,* 525 U.S. 1062, 119 S.Ct. 634, 142 L.Ed.2d 571 (1998); *see also Gilbrook v. City of Westminster,* 177 F.3d 839, 858 (9th Cir. 1999) (holding that an appellate court

reviews evidentiary rulings for abuse of discretion). We may not reverse the trial court's ruling unless it is "manifestly erroneous." *See Desrosiers,* 156 F.3d at 960; *General Elec. Co. v. Joiner,* 522 U.S. 136, 118 S.Ct. 512, 139 L.Ed.2d 508 (1997). An expert witness may base his or her opinion on facts or data "of a type reasonably relied upon by experts in the particular field." FED. R. EVID. 703. It is common sense that certified public accountants reasonably rely on loan agreements to calculate the interest due on loans. Defendants make no argument as to why it was unreasonable for Degnan to rely on loan agreements and promissory notes. Accordingly, we find that the district court's ruling that the bank loan documents were reliable was not "manifestly erroneous."

Defendants do make a variety of arguments about Degnan's qualifications to interpret loan agreements, Degnan's assumptions about the interest rate, and the general accuracy of Degnan's testimony. Defendants did not object to Degnan's testimony at trial on any of these grounds, and therefore they cannot raise these objections on appeal.[5] *See*

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[5] Defendants could possibly have challenged the accuracy of Degnan's testimony through a relevance objection. *See Bradley v. Armstrong Rubber Co.,* 130 F.3d 168, 177 (5th Cir. 1997) ("Even if rule 703 will not require the exclusion of such an unfounded opinion, general principles of relevance will. In other words, an opinion based totally on incorrect facts will not speak to the case at hand and hence will be irrelevant.").

It is not clear, however, that Degnan's testimony was inaccurate, as plaintiffs contend. Degnan testified that he calculated the interest due by selecting the higher of two rates and multiplying the higher rate by 1.5. The loan agreement states:

> If for any reason "THE BORROWER" should fail to pay the required sums to "THE LENDER" in a timely manner, it shall pay to "THE LENDER" default interest on the unpaid balance, equivalent to 1.5 times the yield announced by the Banco de Mexico for the primary issue of 28-day CETES (Treasury Discount Securities) or the C.P.P. (Average Cost of Funds Rate), whichever is higher as of the date when the default interest begins accruing.

(footonote continued)

Masayesva v. Hale, 118 F.3d 1371, 1379 (9th Cir. 1997), *cert. denied sub nom., Hale v. Secakuku,* 522 U.S. 1114, 118 S.Ct. 1048, 140 L.Ed.2d 112 (1998) (failure to make a specific evidentiary objection waives the right to assign error on appeal); FED. R. EVID. 103(a)(1). Moreover, if defendants disagreed with Degnan's testimony at trial, they could have attempted to cast doubt on it by cross- examining Degnan and presenting their own evidence of the amount of interest due.

IV

Rule 59 Motion

Defendants argue that they are entitled to a new trial under Rule 59 because the evidence presented to the jury was insufficient to sustain the damage award. We review a district court's denial of a motion for a new trial for an abuse of discretion. *See Browning-Ferris Indus. v. Kelco Disposal, Inc.,* 492 U.S. 257, 278, 109 S.Ct. 2909, 106 L.Ed.2d 219 (1989); *Marcy v. Delta Airlines,* 166 F.3d 1279, 1282 (9th Cir. 1999). As defendants concede, to rule in defendants' favor, we must find both that there was insufficient evidence for a jury to find that ECG owed over $11 million to BanRural and that there was insufficient evidence for a jury to find that plaintiffs suffered over $15 million in lost profits. Defendants failed to prove that Degnan's testimony as to the amount of liability in the loan agreements was inaccurate or inadmissible. Plaintiffs also presented testimony that BanRural had a viable cause of action under Mexican law

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Defendants argue that this testimony was inaccurate because various notices from BanRural, introduced into evidence at trial, stated that the bank was charging a lower interest rate. Any inconsistency between the default notices and the agreements presented a question of fact for the jury. Thus, the cases cited by defendants for the general proposition that a court must exclude inaccurate expert testimony, even if it is not objected to at trial, are off point because defendants have not shown that Degnan's testimony was inaccurate.

against plaintiffs. Thus, we find that the district court did not abuse its discretion in denying defendants' Rule 59 motion.

V

Rule 60(b)(3) Motion

Defendants' final argument is that the district court erred in denying a Rule 60(b)(3) motion for relief from judgment based on plaintiffs' failure to produce evidence during discovery and their introduction of false testimony at trial. Rule 60(b)(3) permits a losing party to move for relief from judgment on the basis of "fraud, . . . misrepresentation, or other misconduct of an adverse party." FED. R. CIV. P. 60(b)(3). To prevail, the moving party must prove by clear and convincing evidence that the verdict was obtained through fraud, misrepresentation, or other misconduct and the conduct complained of prevented the losing party from fully and fairly presenting the defense. *See Lafarge Conseils et Etudes, S.A. v. Kaiser Cement & Gypsum Corp.*, 791 F.2d 1334, 1338 (9th Cir. 1986); *Jones v. Aero/Chem Corp.*, 921 F.2d 875, 878-79 (9th Cir. 1990). Rule 60(b)(3) "is aimed at judgments which were unfairly obtained, not at those which are factually incorrect." *In re M/V Peacock*, 809 F.2d 1403, 1405 (9th Cir. 1987). The district court denied defendants' Rule 60(b)(3) motion because it found that the plaintiffs did not engage in misconduct and the judgment was not unfairly procured. We review the district court's denial of a Rule 60(b) motion for an abuse of discretion and will reverse "only upon a clear showing of abuse of discretion." *Molloy v. Wilson*, 878 F.2d 313 (9th Cir. 1989); *see also Wilson v. San Jose*, 111 F.3d 688, 691 (9th Cir. 1997); *In re M/V Peacock*, 809 F.2d at 1404.

Defendants contend that plaintiffs engaged in discovery misconduct by not disclosing (1) the pleadings in their litigation with BanRural in a Mexican court; (2) that a Mexican court dismissed the BanRural suit three months before the trial began in this case; and (3) ECG's accounting records. Under Rule 26, litigants are required to provide, without being specifically requested to do so, "a copy of, or a description by category and location of, all documents . . . in

the possession, custody, or control of the party that are relevant to the disputed facts alleged with particularity in the pleadings," and "the documents . . . on which computation [of damages] is based," FED. R. CIV. P. 26(a)(1)(B)-(C). However, the factual allegations in the complaint relied on by the defendants[6] do not satisfy the "alleged with particularity" requirement of Rule 26. Further, the defendant's document requests made under Rule 34 do not specifically refer to litigation between BanRural and De Saracho.[7] While the allegations and document requests might be interpreted as requiring disclosure of the pleadings insofar as they involve plaintiffs' liability to BanRural, the district court found that defendants fell short of proving by clear and convincing evidence that plaintiffs engaged in misconduct. In addition, the district court found that defendants did not prove by clear and convincing evidence that the Mexican court actually dismissed the action. Plaintiffs presented evidence in response to the Rule 60(b) motion that, under Mexican law, an interlocutory ruling does not terminate the litigation and that the ruling was reversed on appeal. With respect to ECG's accounting records, the district court found that plaintiffs did not have actual or constructive possession of the records, that there was no evidence that plaintiffs had access to computer records containing this information, and that there was no evidence that plaintiffs knew Avalli's check was worthless when they created those records. *See Jones,* 921 F.2d at 879 (stating

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[6] Defendants rely on paragraphs of the complaint that allege plaintiffs' liability on the BanRural loans and the diminution in the value of Maria De Saracho's land resulting from ECG's default.

[7] Defendants requested "[a]ll documents which reflect monies borrowed to finance purchase of machinery and equipment for the Culiacan plant which is the subject of plaintiffs' complaint," and "[a]ny and all documents which show, evidence, or relate to monies borrowed by plaintiff for use as operating capital including start-up costs related to the plaintiff's plant which is the subject of plaintiff's complaint on file herein."

that a party may prevail on a Rule 60 motion by showing, *inter alia,* that the nonmoving party "knew, or was charged with knowledge, of the missing document, and had constructive (if not actual) possession of it"). These factual findings were not clearly erroneous and as a result, the district court did not abuse its discretion in concluding that Rule 60(b)(3) relief was not warranted on the basis of discovery misconduct.

Second, defendants argue that plaintiffs introduced false testimony that ECG is indebted to BanRural for more than $11 million. To support this contention, defendants point to new evidence, not presented at trial, purportedly proving that the interest rate provision in the loan documents on which Degnan relied was a mistake and that BanRural actually intended to charge a lower interest rate. The district court held that defendants failed to prove by clear and convincing evidence that "BanRural ever informed [plaintiffs] of its election to accrue interest at a rate never agreed upon by the parties and never the subject of any modification of the loan documents." Defendants present no evidence that plaintiffs knew that BanRural did not intend to charge the interest rate set out in the loan documents. Thus, we find that the district court did not abuse its discretion in ruling that Rule 60 relief was not warranted for this reason.

VI

We affirm the district court's denial of defendants' motion *in limine* seeking dismissal on the ground that plaintiff ECG's lacked authorization to bring suit, motion to strike the testimony of plaintiffs' expert witness, Rule 59 motion for a new trial, and Rule 60(b) motion for relief from judgment.

AFFIRMED.

BRIGHT, Circuit Judge, dissenting:

In this case, the Plaintiffs recovered a verdict of 12.5 million dollars. Included in the damage calculation was testimony of the Plaintiffs' expert, Stephen Degnan, who calculated that the Plaintiffs owed BanRural approximately

11.4 million dollars. Over objection, the trial court admitted this evidence that the jury could use in measuring the Plaintiffs' damages.

It is now known that BanRural's claim, calculated six months after trial, does not exceed 5.5 million dollars. In my view, one does not prove a bank debt such as this one by having an expert witness testify as to the estimated amount of the loan. A bank's debtor should either testify as to the amount of the bank's demand or produce evidence from the bank of the amount of the debt. Neither was done here.

The trial court improperly admitted the expert testimony establishing an inflated bank debt that produced a windfall for the Plaintiffs' damages. Expert testimony based on incorrect underlying facts should be excluded. *See United States v. City of Miami,* 115 F.3d 870, 873 (11th Cir.1997); *see also Bradley v. Armstrong Rubber Co.,* 130 F.3d 168, 177 (5th Cir.1997).

I would grant the Defendant a new trial on damages unless the Plaintiffs would, by remittitur, accept an award reducing the jury award of damages by 2.5 million dollars.

APPENDIX B

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF CALIFORNIA

MARIA TERESA DE SARACHO; EUREKA CANNERS GROUP, S.A., a corporation formed under the laws of Mexico; and EUREKA MEXICANA, S.A., a corporation formed under the laws of Mexico, Plaintiffs,

v.

CUSTOM FOOD MACHINERY, INC., a California corporation; RON McNIEL, SR., FRED AVALLI, and DOE 1 through DOE 25, inclusive, Defendants

And Related Cross-Claim

No C-95 20854 WAI

[Filed July 29, 1997]

JUDGMENT PURSUANT TO JURY VERDICT

Trial Date: June 23, 1997

Judge: Hon. William A. Ingram

This action came on regularly for trial by jury on June 23, 1997 in the above-entitled court. William J. Keegan of the Keegan Law Firm appeared for Plaintiffs Maria Teresa De Saracho, Eureka Canners Group, and Eureka Mexicana. Craig Needham and Anne Jones of Liccardo, Rossi, Sturges & McNeil appeared for Defendant Fred Avalli. Dale Dawson of Dawson, Passafume & Bowden appeared for Defendants Ron McNiel, Sr. and Custom Food Machinery, Inc.

Evidence, both oral and documentary, was presented by all parties. On July 24, 1997 the jury made its findings and rendered its verdict as indicated on the "Jury Verdict" form

returned by the jury. Accordingly, pursuant to the jury's verdict, as indicated by the "Jury Verdict" form as contemplated by the jury,

IT IS HEREBY ORDERED, ADJUDGED, AND DECREED that

1. Plaintiffs Maria Teresa De Saracho, Eureka Canners Group, S.A. de C.V., and Eureka Mexicana, S.A. de C.V. shall recover from Defendants Fred Avalli, Ron McNiel, Sr., and Custom Food Machinery, Inc., jointly and severally, the total sum of $12,516,000.00, exclusive of costs;

2. Cross-Complainant Custom Food Machinery, Inc. shall recover nothing on its Cross-Complaint against Eureka Canners Group, Inc. and First Western Marketing, Inc.

Dated: July 29, 1997.

/s/ William A. Ingram
WILLIAM A. INGRAM
UNITED STATES DISTRICT
COURT JUDGE

APPENDIX C

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF CALIFORNIA

MARIA TERESA DE SARACHO; EUREKA CANNERS GROUP, S.A., a corporation formed under the laws of Mexico; and EUREKA MEXICANA, S.A., a corporation formed under the law of Mexico, Plaintiffs,

v.

CUSTOM FOOD MACHINERY, INC., a California corporation; RON McNIEL, SR., FRED AVALLI, and DOE 1 through DOE 25, inclusive, Defendants

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No C-95 20854 WAI

San Jose, California

Wednesday July 9, 1997

Appearances:

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[The following is an excerpt from pages 1697-98, 1720-25, and 1727 of the reporter's transcript of the trial proceedings occurring on July 9, 1997. The entire trial transcript is contained in the record on appeal in the Ninth Circuit Court of Appeals.]

[1697] Mr. Needham: Excuse me one second. I have an objection to this expert relying on these documents. I know an expert can — can rely on hearsay, but it has to be reliable. And the status of the evidence is that none of these documents are in evidence for the proof of the matter stated. Therefore, this expert's going to be relying upon basically hearsay documents for the truth of what they have to say. And I'll never have an opportunity to cross-examine.

Mr. Keegan: That's completely incorrect. All the loan documentations are in for the truth of the [1698] matter. That's what he looked at. That's what he had interpreted.

Mr. Neeham: I believe Your Honor admitted them for the limited purpose.

Mr. Keegan: Not the loan documents.

The Court: Overruled.

You may answer.

. . . .

[1720] The Court: Go right ahead, please.

Mr. Needham: Yes, Your Honor. Thank you.

I'm holding in my hands, Your Honor — Actually so I can have the record on this, may I mark these items, Your Honor?

The Court: Sure.

Mr. Needham: I'm not sure how — I don't agree that they go in evidence. I would like them marked for the record.

The Court: All right.

Mr. Keegan: Why don't we find the corresponding numbers.

Mr. Needham: I got it. 513 would be the note that he has written 1.8 million on.

(Exhibit 513 marked for identification.)

Mr. Needham: This is a Spanish document, Your Honor.

The Court: All right.

[1721] Mr. Needham: And then 514 would be the 935,000.

(Exhibit 514 marked for identification.)

Mr. Needham: And 515 would be the 500,000.

(Exhibit 515 marked for identification.)

The Court: Those are what, notes?

Mr. Needham: They are — I can tell you exactly what they are, Your Honor, although —

Mr. Keegan: I can.

Mr. Needham: I want —

The Court: I — just so we can identify them, whether it's right or not.

Mr. Needham: They're notes. And they correspond to items that were put into evidence for a limited basis.

Mr. Keegan: These are not notes, Your Honor. These are the notices from the bank in late April, early May saying the loan is in default.

The Court: Notice of Default?

Mr. Keegan: I think where counsel's going, maybe we can shortcut it. Mr. Degnan actually has the loan agreements themselves, the big thick loan agreements which state the interest rate.

Mr. Needham: Well, he finished with his witness. I'm now making a motion to strike based upon [1722] what's happened so far with this witness. I — I don't know if we're opening testimony here or not.

The Court: If — if you're going to give him a chance to reopen — if the — if the point that you're about to make requires that he at least have the chance to reopen — I mean, it's just like moving for non-suit. You don't grant one without a chance to reopen.

For whatever it's worth on the motion you're about to make, I wanted to explain to you — to the record the reason that I ruled as I did on what an expert can rely on. And whether or not these documents that he relied on were admitted for a limited purpose or not, in my view, it makes absolutely no difference. An expert is not — the fact that they may be in evidence for some purpose does not alter an expert's ability to rely on documents that are hearsay, providing they have some index of reliability. And in this instance I have no difficulty in feeling that these documents have some index of reliability for what they purport to be.

With that in mind, go ahead. If that's a part of your motion, that's my ruling.

Mr. Needham: I'm anticipating a big loss based upon what you said. If I could just put in the record?

The Court: Yes. I want you to do that.

[1723] Mr. Needham: Because I — the document that this witness relied on $1.8 million is Exhibit 513 which is not in evidence. And it corresponds to Exhibit 402-E which is — Mr. Keegan is correct — is the notice from the bank on April 26, '95, and that that was admitted for a limited purpose. The document — the Spanish document for 935,000 which is marked as 514 is the same in the English translation as 404-E which the Court had previously admitted

for limited purposes. And the document this witness relied upon, the Spanish version of 500,000, is marked Exhibit 513. And that is the same as Exhibit 403 which was admitted for a limited purpose by the Court.

And the Court has already indicated its ruling with respect to — I — I will stand on my position.

The Court: Yeah.

Mr. Needham: With all due respect.

The Court: You may very well be correct. That's my view of it. I just wanted the record to know that.

Le me ask you, I don't have in mind all of the — the multiple of exhibits that have been offered in this case right now. Do I gather that the documents which created the purported liability in this case are not in evidence?

[1724] Mr. Needham: No. They are. I — I misspoke, Your Honor. And I want to — there are other documents that reflect these notes that are in evidence without a limiting instruction.

The Court: Well, are the promissory notes themselves in evidence?

Mr. Keegan: Yes, Your Honor.

The Court: All right.

Mr. Keegan: As are all the loan agreements.

The Court: Okay.

Mr. Keegan: It's my recollection that what the witness testified to was that he looked at the loan agreements and that he had somebody interpret that — that he could not have anybody interpret the interest rate statement in this because there is none.

The Court: There are English translations of the promissory notes and the security documents that the jury can read them too; is that right?

Mr. Keegan: That's right. It's all in evidence.

The Court: At least the English translations are in evidence without just picking and choosing. But the whole thing is in evidence, correct?

Mr. Keegan: We have — we have three packets of promissory notes. And we have three loan agreements [1725] all in evidence for an unlimited purpose.

The Court: Fine. That's all I wanted to know.

Anything further?

Mr. Needham: Yes, Your Honor. There is — I think Mr. Keegan can correlate this.

There is in evidence 386 which is an English version that related to the five hundred thousand dollars which relates to the March '94 loan and there the nine thirty-five loan. Those are in evidence in English, Your Honor. I couldn't pull my —

Mr. Keegan: It's 129 which is in evidence.

Mr. Needham: I just wanted to have the record clear when somebody looks at this. Yes, 129 is the promissory note that is in evidence translated in English on the 1.8.

Mr. Keegan: My recollection is that they also state the promissory notes, the basic interest rate.

Mr. Needham: Those documents will speak for themselves when I take a look at the testimony.

. . . .

[1727] The Court: All right. Objection's overruled.

Mr. Needham: All right, Your Honor.

APPENDIX D

UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

MARIA TERESA DE SARACHO, EUREKA CANNERS GROUP, S.A., a corporation formed under the laws of Mexico; EUREKA MEXICANA SA, a corporation formed under the law of Mexico, Plaintiffs-Appellees,

v.

CUSTOM FOOD MACHINERY INC., a California corporation; RON McNEIL, SR., Defendants-Appellants, and FRED AVALLI, and DOE 1 through DOE 25, inclusive, Defendant-Appellant.

Nos. 98-15003, 98-15007, 98-17051

[Filed April 17, 2000]

Order

Before: BRIGHT,[1] PREGERSON, and W. FLETCHER, Circuit Judges

Appellants' petition for rehearing is denied.

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[1] The Honorable Myron Bright, Circuit Judge for the Eighth Circuit Court of Appeals, sitting by designation.

(2)

Supreme Court, U.S.
FILED
AUG 18 2000
CLERK

No. 00-104

In The

Supreme Court of the United States

CUSTOM FOOD MACHINERY, INC. and
RON McNIEL, Sr.,

Petitioners,

vs.

MARIA TERESA DE SARACHO,
EUREKA CANNERS GROUP, S.A., and
EUREKA MEXICANA, S.A.,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

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QUESTIONS RESTATED

1. Does Federal Rule of Evidence 703 require a trial court to make a determination that an expert's reliance on documents which have been stipulated into evidence was reasonable?

2. Is the trial court required to make an explicit finding as to the reasonableness of an expert's sources, and if so, is the trial court's determination that those sources have an adequate "index of reliability" sufficient?

3. Does a non-specific objection to the reliability of an expert's information sources trigger a duty in the trial court to review all the evidence and anticipate a specific reliability argument that was not made until after the trial?

CORPORATE DISCLOSURE STATEMENT

Pursuant to Supreme Court Rule 29.6, Respondent Eureka Mexicana, S.A. states that it has no parent corporation and that no publicly held company owns 10% or more of its stock.

Pursuant to Supreme Court Rule 29.6, Respondent Eureka Canners Group, S.A. states that it has no parent corporation and that no publicly held company owns 10% or more of its stock.

TABLE OF CONTENTS

Page

QUESTIONS RESTATED i

CORPORATE DISCLOSURE STATEMENT ii

STATEMENT 1

REASONS TO DENY THE WRIT 6

I. PETITIONERS HAVE NOT PRESERVED FOR THIS COURT'S REVIEW THE ISSUE THEY RAISE 6

II. THERE IS NO POST-*DAUBERT* SPLIT CONCERNING THE TRIAL COURT'S ROLE WHERE AN EXPERT RELIES ON OTHERWISE INADMISSIBLE EVIDENCE 7

III. THE PRE-*DAUBERT* SPLIT IDENTIFIED BY PETITIONERS HAS NO APPLICATION WHERE THE BASIS OF THE EXPERT'S OPINION HAS BEEN STIPULATED INTO EVIDENCE 11

IV. THE TRIAL COURT'S EXPRESS FINDING OF RELIABILITY IS SUFFICIENT UNDER ANY STANDARD 13

CONCLUSION 14

TABLE OF AUTHORITIES

Pages

CASES

Daubert v. Merrell Dow Pharmaceuticals, Inc.
509 U.S. 579 (1993) ..... *passim*

DeLuca v. Merrell Dow Pharmaceuticals
911 F.2d 941 (3rd Cir. 1990) 8

General Electric Co. v. Joiner, 522 U.S. 137 (1997) 4

Indian Coffee Corp. v. Proctor & Gamble Co.
752 F.2d 891 (3rd Cir. 1985) 8

In re Japanese Elec. Prods.
723 F.2d 238 (3rd Cir. 1983), *rev'd in part sub nom.* Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574 (1986), *on remand* 807 F.2d 44 (3rd Cir. 1986), *cert. denied*, 481 U.S. 1029 (1987) 8

In re Paoli Railroad Yard PCB Litigation
35 F.3d 717 (3rd Cir. 1994), *cert. denied*, 513 U.S. 1190 (1995) 8

Mannino v. Int'l Mfg.
650 F.2d 846 (6th Cir. 1981) 10

McKendall v. Crown Control Corp.
122 F.3d 803 (9th Cir. 1997) 10

Moore v. Ashland Chemical, Inc.
126 F.3d 679 (5th Cir. 1997), *rev'd en banc on other grounds*, 151 F.3d 269 (5th Cir. 1998) 9

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155 F.3d 1130 (9th Cir. 1998) 10

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TABLE OF AUTHORITIES – Continued

Page(s)

STATUTES AND RULES

Federal Rules of Evidence
Rule 103 7

Rule 703 ..... *passim*

SECONDARY SOURCES

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STATEMENT

At trial Petitioner Ron McNiel, President of Custom Food Machinery, admitted he knew he was participating in a fraud when he supplied blank pre-signed Custom Food Machinery invoices to his co-conspirators – invoices that were then filled in with a completely false description of a $2.15 million transaction.[1] Respondents (plaintiffs below) were misled into paying premium prices for antiquated, inoperable cannery equipment, rather than the high quality equipment petitioners fraudulently represented they were selling. As an additional consequence of the fraud, plaintiffs borrowed U.S. dollars from a Mexican bank under loan contracts that were pegged to the value of the Mexican peso. Thus, when the junk equipment incapacitated the cannery, and the peso-to-dollar exchange rate slid precipitously as a result of a government devaluation, the interest rates on plaintiffs' loans soared, and plaintiffs had no functioning cannery business with which to repay.

When this diversity fraud case went to trial, plaintiffs' claimed damages exceeding $27 million.[2]

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[1] Q. Forget Exhibit 14 for a second. You understood when you handed out the blank invoices that someone was going to use those to mislead someone else, right?

A. Yes.

P-ER 2204 (McNiel trial testimony). "P-ER" refers to the excerpts of record filed by plaintiffs/respondents in the court of appeals.

[2] In addition to the $11.3 million bank debt, plaintiffs presented uncontested evidence that as a result of the fraud: one of the corporations victimized by petitioners' fraud had lost more than $15 million in anticipated profits; another plaintiff

In a compromise general verdict, the jury awarded $12.5 million.

One component of the amount claimed by plaintiffs was $11.3 million – the balance due on the Mexican bank loans as of the time of the trial. This amount was calculated by plaintiffs' expert witness, a Certified Public Accountant. The CPA's testimony was simple and straightforward; and it was not based on any "assumptions"[3] at all. He multiplied the interest rates set forth in loan agreements and promissory notes, all of which had been properly authenticated and admitted into evidence (without objection) much earlier in the trial, by the loan principal in order to calculate the balance due. There has never been any contention that the CPA's reading of the interest provisions in the loan documents was incorrect, or that the simple arithmetic he performed was flawed in any way.

In fact, the defendants introduced no evidence and made no argument at trial contradicting the CPA's computations. They offered no alternative interest rate calculation. Their only contention at trial was that the loan agreements and promissory notes were, for some unstated reason, an unreliable basis for the expert's opinion about the interest rate called for by the loan.

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corporation was put out of business entirely; numerous non-bank debts and expenses also resulted from the deception; and the individual plaintiff who had guaranteed all of the bank loans was suffering from severe emotional distress.

[3] Pet., at 3.

In overruling defendants' objection, the trial court found that even if the loan documents had not been admitted into evidence (as defendants mistakenly contended for a while), they were sufficiently reliable to be the basis of an expert's testimony about the applicable interest rate:

> And in this instance, I have no difficulty in feeling that these loan documents have some index of reliability for what they purport to be.[4]

Eight months after the trial was over, the defendants filed an unsuccessful motion for relief from judgment under Federal Rule of Civil Procedure 60(b)(3). At that time the defendants revealed that they had some hearsay evidence (not introduced at trial) indicating that the Mexican bank might be willing to apply a lower interest rate than the one reflected in all the loan documents and that the bank might settle its claims with plaintiffs for less than the full amount due on the loans. Although they had an opportunity to do so, the defendants declined to take any post-trial depositions to authenticate the evidence they had regarding the Mexican bank's position.

In the Ninth Circuit, defendants claimed that there was a "wild inconsistency" between the rate the bank applied in its April 1995 notices and the rate the CPA used for subsequent periods.[5] The defendants never complained on their appeal, however, that the trial court had

---

[4] P-ER 2238, reprinted in Petitioners' App., at 19a.

[5] It is not surprising that this "inconsistency" was not noticed or mentioned until long after the trial. The supposed "inconsistency" is simply a frivolous post-trial argument that the interest rate the bank utilized in the period immediately *before* the peso's slide accelerated in early 1995, differs from the

failed to make an independent finding about the reliability of the loan documents the CPA used to calculate interest payable. Instead, they argued that the CPA's testimony should have been excluded based on: (a) the post-trial argument that the interest rates called for in the loan documents were inconsistent with the rates of interest applied in the Mexican bank's April 1995 notices; and (b) the post-trial discovery of evidence that the bank might be willing to negotiate the balance due and use a different interest rate.

In a ruling petitioners do not challenge, the Ninth Circuit upheld the denial of Rule 60(b) relief. Petitioners' App., at 12a. Thus, the court found no reason to take into consideration any of the evidence adduced after judgment. Based on the trial record, the Ninth Circuit upheld the admission of the CPA's testimony as a permissible exercise of discretion, citing this Court's decision in *General Electric Co. v. Joiner*, 522 U.S. 137 (1997). Petitioners' App., at 7a to 7b.

The dissenting judge in the court of appeals, however, based his decision to remit $2.5 million of the judgment (authorizing a total award to plaintiffs of $10

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rate the accountant used for the time periods *after* the peso plummeted. At trial, the CPA did compare those rates and testified that the early bank statements *confirmed* his reliance on the interest provisions stated in the loan documents: "I also checked them by looking at the statements that I did have from the bank. In other words, the bank had provided some early statements, just hadn't provided current statements. I checked to make sure that the methodology that was explained to me was accurate by recalculating it in the early years, 1995." P-ER 2227.

million) on a willingness to take into consideration hearsay evidence first offered *after* judgment as part of the Rule 60(b) motion. Moreover, the dissenting judge would have imposed a specific requirement on the manner in which a plaintiff could prove the amount due on a loan. Petitioners' App., at 13a. More significantly for purposes of this petition, the dissenting judge did not identify any error on the part of the district court in failing to carry out any *Daubert* gatekeeping function.

In this Court, petitioners read the Ninth Circuit decision as illustrative of a split between the circuits on Federal Rule of Evidence 703: with a "liberal" faction holding that a district court must yield to the actual practices of experts in relying on otherwise inadmissible evidence; while a "restrictive" camp requires the trial court to make its own determination on whether that reliance is reasonable.

There does not appear to be any post-*Daubert*[6] controversy on this issue, however. Two of the three circuits that were formerly in the "liberal" faction have now recognized that *Daubert* precludes their earlier interpretation. The third, the Sixth Circuit, has not yet had an opportunity to revisit the subject. There is no reason to think the Sixth Circuit remains in the "liberal" faction. No opinion published in any circuit after *Daubert*, least of all the opinion in *this* case, can be read as endorsing the "liberal" interpretation.

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[6] *Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579 (1993).

Even if the pre-*Daubert* split were to be resuscitated by some circuit's adoption of the "liberal" interpretation tomorrow, that controversy would have no application to this case anyway. First, petitioners have not preserved the issue they tender for this Court's review. Second, the split of yesteryear involved different views of a trial court's duties where the expert relies on *in*admissible evidence; here the basis of the CPA's testimony had been stipulated to be admissible evidence months before the CPA ever took the witness stand. And third, the trial judge in this case independently evaluated the reliability of the data relied on by the expert and then made an explicit finding that it was reliable; even the most "restrictive" views of Rule 703 do not require anything more than that.

REASONS TO DENY THE WRIT

I. PETITIONERS HAVE NOT PRESERVED FOR THIS COURT'S REVIEW THE ISSUE THEY RAISE.

The Ninth Circuit did not consider and decide the legal issue presented by the petition. That is because petitioners did not brief either Rule 703 or *Daubert* in the court of appeals. There was no mention made about a "liberal" or a "restrictive" approach to Rule 703. Nor was there any contention raised that the district court had yielded to the expert's own practices, thereby failing to carry out its duty to independently consider the trustworthiness of the information relied upon. This Court, as a matter of policy, does not decide questions that were not presented to the court of appeals for consideration.

Additionally, it was not until long after the trial was over that petitioners first suggested that there was any "inconsistency" between the interest rates described in the loan documents and the rates used by the bank in the early years of the loan. A trial judge is not obligated to anticipate post-trial factual arguments in ruling on the admissibility of evidence. As the Ninth Circuit observed, by failing to specifically object in the district court (as required by Federal Rule of Evidence 103) petitioners waived all such evidentiary arguments. Petitioners' App., at 8a. This lack of proper, specific objection makes the case fact-bound and would require affirmance without regard to the existence of any circuit court conflict.

Additionally, in arguing that the result below was flawed, the petition relies heavily on hearsay that was not proffered until *after judgment*, during Rule 60(b) proceedings. *See Pet.* at 4. But the denial of Rule 60(b) relief is not challenged in the petition. Questionable evidence, which was not before the district court during trial, is not available after the fact to attack the admission of the CPA's testimony.

II. THERE IS NO POST-*DAUBERT* SPLIT CONCERNING THE TRIAL COURT'S ROLE WHERE AN EXPERT RELIES ON OTHERWISE INADMISSIBLE EVIDENCE.

Petitioners report a "pervasive conflict" regarding an expert's use of otherwise inadmissible evidence under Federal Rule of Evidence 703.[7] They cite four secondary

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[7] Pet., at 4.

authorities as having recognized this split.[8] However, none of the "liberal" cases cited, either in the petition or in any of those secondary authorities, was decided *after Daubert* clarified the field in 1993.

Early cases from the Third Circuit were the ones most frequently cited in the past as illustrative of a "liberal" interpretation allowing the practices of experts in the field to dictate admissibility.[9] But in 1994 the Third Circuit recognized that "our former view is no longer tenable in light of *Daubert*," and it agreed that Rule 703 requires that "the judge must conduct an independent evaluation into reasonableness."[10]

One 1989 Fifth Circuit decision is also cited in petitioners' secondary authorities as illustrating the "liberal"

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[8] Pet., at 5-6, and 12-13, citing Epps, *Clarifying the Meaning of Federal Rule of Evidence 703*, 36 B.C. L. Rev. 53, 75-76 (1994) ("Epps"); Imwinkelried, *Developing a Coherent Theory of the Structure of Federal Rule of Evidence 703*, 47 Mercer L. Rev. 447, 464 (1996) ("Imwinkelried"); 2 M.H. Graham, *Handbook of Federal Evidence*, § 703.1, p. 105, n.14 (4th ed. 1996) ("Graham"); and 3 Mueller & Kirkpatrick, *Federal Evidence* § 357 (2d ed. 1994) ("Mueller & Kirkpatrick").

[9] *See, e.g.*, Epps, at 76, n.99, citing: *In re Japanese Elec. Prods.*, 723 F.2d 238, 276-277 (3rd Cir. 1983), *rev'd in part sub nom. Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574 (1986), *on remand*, 807 F.2d 44 (3rd Cir. 1986), *cert. denied*, 481 U.S. 1029 (1987); *DeLuca v. Merrell Dow Pharmaceuticals*, 911 F.2d 941, 952 (3rd Cir. 1990); and *Indian Coffee Corp. v. Proctor & Gamble Co.*, 752 F.2d 891, 897 (3rd Cir. 1985). *See also* Graham, at 105-106, n.14 (citing the same cases); and Mueller & Kirkpatrick, § 357, p. 679-680, n.12 (citing two of the same cases).

[10] *In re Paoli Railroad Yard PCB Litigation*, 35 F.3d 717 (3rd Cir. 1994), *cert. denied*, 513 U.S. 1190 (1995).

approach.[11] But *Daubert* has apparently caused the Fifth Circuit to also abandon the "liberal" camp:

> Accordingly, the trial judge as gatekeeper has a duty under Rule 703 to determine whether such facts and data not admitted in evidence are of the type customarily relied upon by experts in the field and whether such reliance is reasonable.[12]

The Ninth Circuit opinion in *this* case is certainly no authority for a "liberal" approach to Rule 703. Petitioners never even mentioned *Daubert* in the trial court or in their appellate court briefing; nor did they allude to any split of authorities under Rule 703; nor did they suggest that the trial court had failed to follow a "restrictive" interpretation. Because the issue was never raised, the Ninth Circuit never saw any reason to take either side of the now-rapidly-healing split. However, in answer to the contention that was advanced below, that the trial court had abused its discretion by admitting the expert testimony, the Ninth Circuit backed up the trial court's express reliability finding with its own observation on the reasonableness of the expert's reliance:

> It is common sense that certified public accountants reasonably rely on loan agreements to calculate the interest due on loans.[13]

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[11] *See, e.g.*, Epps, at 76, n.99, citing: *Peteet v. Dow Chem.* Co., 868 F.2d 1428, 1432 (5th Cir. 1989), *cert. denied*, 493 U.S. 935 (1989). *See also* Graham, at 105-106, n.14 (citing the same case).

[12] *Moore v. Ashland Chemical, Inc.*, 126 F.3d 679, 691 (5th Cir. 1997), *rev'd en banc on other grounds*, 151 F.3d 269 (5th Cir. 1998).

[13] Petitioners' App., at 8a.

Petitioners also misdescribe the Ninth Circuit's other jurisprudence. According to petitioners, the "restrictive" approach has "only" gained acceptance in the Ninth Circuit in a dissenting opinion. This is petitioners' parenthetical description of what they say is that dissenter's lonesome recognition that a "restrictive" approach is required:

> (noting that the Supreme Court holding in *Daubert* stressed that 'in ruling on admissibility, trial judges are gatekeepers and should pay particular attention to the reliability of the expert and his or her testimony' (citations omitted)).[14]

But the language petitioners quote does not "only" appear in a dissenting opinion. In actuality, the dissenter in that case was quoting from a *unanimous* Ninth Circuit opinion, something which would have been obvious if petitioners had not omitted the full citation from their petition in this Court.[15] So the language petitioners quoted actually indicates that the "restrictive" approach has gained acceptance, not "only" in a dissenting opinion, but by a unanimous Ninth Circuit panel as well.

That leaves only one nineteen year old Sixth Circuit case as the single still-standing example of the "liberal" fork of the Rule 703 split.[16] Judging from what has happened in every other circuit since 1993, the pre-*Daubert*

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[14] Pet., at 10-11, citing *Sementilli v. Trinidad Corp.*, 155 F.3d 1130 (9th Cir. 1998) (B. Fletcher, J., dissenting).

[15] *Sementilli v. Trinidad Corp.*, 155 F.3d 1130, 1141 (9th Cir. 1998) (B. Fletcher, J., dissenting), attributing the quoted language to *McKendall v. Crown Control Corp.*, 122 F.3d 803, 806-07 & n.1 (9th Cir. 1997).

[16] *Mannino v. Int'l Mfg.*, 650 F.2d 846, 853 (6th Cir. 1981).

split will be completely healed once the Sixth Circuit has an opportunity to address the question with *Daubert* as guidance.

In short, no active conflict requires this Court's attention.

III. THE PRE-*DAUBERT* SPLIT IDENTIFIED BY PETITIONERS HAS NO APPLICATION WHERE THE BASIS OF THE EXPERT'S OPINION HAS BEEN STIPULATED INTO EVIDENCE.

The pre-*Daubert* split which is the subject of this petition concerned the courts' interpretation of the second sentence of Rule 703, which departed from the practice at common law by permitting an expert to rely on hearsay or otherwise inadmissible sources:

> If of a type reasonably relied upon by experts in the particular field in forming opinions or inferences upon the subject, the facts or data need not be admissible in evidence.[17]

That sentence, the now-dated controversy about whether the court or the expert has the final word on what has been "reasonably relied upon," and the authorities cited in the petition, are only concerned with an expert who bases her opinion on otherwise *inadmissible* information.[18]

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[17] Federal Rule of Evidence 703.

[18] *See, e.g.*, Epps, *supra*, 36 B.C. L. Rev., at 76 ("This Article argues that Rule 703 imposes an active obligation on courts to determine the reasonableness of an expert's reliance on otherwise *inadmissible* facts or data.") (emphasis added).

The split identified by petitioners has nothing to do with the common law practice of allowing expert testimony based on documents that have been previously admitted into evidence.[19] Here the loan documents that provided the basis of the expert's testimony were all stipulated into evidence two months before the trial began.[20] By stipulating to their admission, the defendants were agreeing that the loan documents were sufficiently reliable for the jury to consider and utilize in reaching a verdict. Consequently, it was unnecessary for anyone to act as "gatekeeper" and preclude that information from getting to the jury through the medium of expert testimony. The defendants had already agreed that the evidence could pass through the "gate;" and the jury already had it. The jury could have performed an interest calculation based on the terms of the promissory notes all by itself; or plaintiffs' counsel could have illustrated the necessary arithmetic in his closing argument. In such circumstances, it was certainly proper for an expert witness to take such evidence into account.

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[19] Epps, *supra*, 36 B.C. L. Rev., at 56-57 ("The common law admitted opinions based on facts or data personally observed as well as opinions based on facts or data presented at trial.").

[20] In a pre-trial order, the district court required the parties to provide written objections to any documentary evidence offered by a date certain. *See* U.S.D.C. Dkt. No. 49. All of the loan documents were properly designated by plaintiffs (Dkt. No. 48); and defendants never registered any objection to any of them. When the loan documents were later offered at trial, petitioners confirmed that they had "no objection" to their admission. *See, e.g.*, Respondents' Appendix attached hereto, at 1a to 4a.

Nothing required the trial judge to anticipate a post-trial argument and then usurp the jury's function of placing whatever reliance it deemed appropriate on documents the defendants conceded were admissible into evidence. Nothing in Rule 703, *Daubert*, or any circuit court decision draws into doubt the evidentiary rulings of the district judge in this case.

IV. THE TRIAL COURT'S EXPRESS FINDING OF RELIABILITY IS SUFFICIENT UNDER ANY STANDARD.

It is not clear whether the now practically-unchallenged "restrictive" interpretation of Rule 703 would require the district court to make an *explicit* finding on the reasonableness of an expert's reliance on inadmissible sources. The Second Circuit did not think so:

> We decline, however, to shackle the district court with a mandatory and explicit trustworthiness analysis . . . In fact, we assume that the district court consistently and continually performed a trustworthiness analysis sub silento of all evidence introduced at trial. We will not, however, circumscribe this discretion by burdening the court with the necessity of making an explicit determination for all expert testimony.[21]

In this case, the district court made an explicit finding that the loan documents had a sufficient "index of reliability" to provide the basis of the CPA's opinion,

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[21] *United States v. Locascio*, 6 F.3d 924, 938-939 (2d Cir. 1993), *cert. denied*, 511 U.S. 1070 (1994).

irrespective of whether they had been admitted or not.[22] So whether there is a split in the circuits or not is completely irrelevant here, where the district court complied with *any* standard that could arguably apply.

CONCLUSION

There was no "undeniable windfall" in this case. The jury's $12.5 million compromise verdict was fully justified, either by reference to the CPA's calculation of the $11.3 million bank debt, or by considering the $16 million in other damages incurred by plaintiffs as a result of petitioners' admitted fraud. Nor is there any continuing split in the interpretation of Rule 703. And even if there were, such an issue is immaterial to the outcome of this case.

[22] P-ER 2238, reprinted at Petitioners' App., at 19a.

The petition for writ of certiorari should be denied.

DATED: August 18, 2000

Respectfully submitted,

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RESPONDENTS' APPENDIX

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF CALIFORNIA

MARIA TERESA DE SARACHO; EUREKA CANNERS GROUP, S.A., a corporation formed under the laws of Mexico; and EUREKA MEXICANA, S.A., a corporation formed under the laws of Mexico, Plaintiffs,

v.

CUSTOM FOOD MACHINERY, INC., a California corporation; RON McNIEL, SR., FRED AVALLI, and DOE 1 through DOE 25, inclusive, Defendants

---

No. C-95 20854 WAI

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[The following is an excerpt from pages 373-374, 541 and 543 of the transcript of the trial proceedings occurring on June 26, 1997. The entire trial transcript is contained in the record on appeal in the Ninth Circuit Court of Appeals.]

[373] Q. What is 388, and what's 388-e?

Mr. Keegan: Your Honor, I move in 129 and 129-e.

The Court: All right. You already did.

Mr. Keegan: I'm sorry.

(Exhibit 129, 129-e received in evidence.)

The Witness: This is another – another loan for Eureka Canners Group where I – I guarantee – I guarantee the loan. And the amount is nine thousand thirty-five – thirty-five hundred – I'm sorry, nine hundred thirty-five thousand dollars.

Mr. Keegan: Q. Okay.

A. Excuse me. My English is very bad.

Q. And I would like to hand you a third and final loan, which has Exhibits 386 and 386-e. Tell me what that is.

A. This is another loan that was given to Eureka Canners Group in which I signed – I co-signed. I responsible for these. And the amount is five thousand – five hundred thousand dollars.

Mr. Keegan: Your Honor, I would like to move in 386 and 386-e.

[394] The Court: Any objection?

Mr. Needham: I have no objection to the English translations going in of those documents. And was 129-e already admitted? I have no objection to that.

The Court: Yeah, yeah.

Mr. Needham: Just the English documents with respect to that.

(Exhibit 386, 386-e received in evidence.)

* * *

[541] Mr. Needham: So 126, 381, and 389?

Mr. Keegan: That's exactly right.

Mr. Needham: All right.

Mr. Keegan: Q. What are these documents?

A. That's are – these are – you call payable notes.

Q. Promissory notes?

A. Promissory notes.

* * *

[543] Mr. Keegan: And, Your Honor, in the meantime, Your Honor, I would like to move in 389, 381 and 126.

The Court: Any objection to those three?

Mr. Needham: No.

The Court: They will be admitted.

Mr. Keegan: Thank you, Your Honor.

(Exhibits 126, 126-e, 381, 381-e, 389, and 389-e received in evidence.)

(3)

No. 00-104

Supreme Court, U.S.
FILED
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CLERK

In the Supreme Court of the United States

CUSTOM FOOD MACHINERY, INC. and RON MCNIEL, SR.,

Petitioners,

v.

MARIA TERESA DE SARACHO, EUREKA CANNERS GROUP, S.A. and EUREKA MEXICANA, S.A.,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

REPLY BRIEF FOR PETITIONERS

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TABLE OF CONTENTS

Page

REPLY BRIEF FOR PETITIONERS 1

A. The Circuits Are in Conflict. 2

B. The Rule 703 Analysis Does Not Turn on Whether the Underlying Facts, Data and Opinions Have Been Admitted. 5

C. Petitioners Have Preserved the Issue for Review. 6

D. Plaintiffs Misstate the Record. 7

CONCLUSION 9

TABLE OF AUTHORITIES

Page(s)

Cases:

Bauman v. Centex Corp., 611 F.2d 1115 (5th Cir. 1980) 5

Daubert v. Merrell Dow Pharmaceuticals, Inc., 509 U.S. 579 (1993) ..... passim

In re "Agent Orange" Product Liability Litigation, 611 F. Supp. 1223 (E.D.N.Y. 1985), *aff'd*, 818 F.2d 187 (2d Cir. 1987) 1

Manniano v. Int'l Mfg., 650 F.2d 846 (6th Cir. 1981) 2, 3

McKendall v. Crown Control Corp., 122 F.3d 803 (9th Cir. 1997) 4

Richards v. Jefferson County, 517 U.S. 793 (1996) 6

Sementilli v. Trinidad Corp., 155 F.3d 1130 (9th Cir. 1998) 4

Trepel v. Roadway Express, 194 F.3d 708 (6th Cir. 1999) 3

Rules:

Federal Rules of Civil Procedure

Rule 46 6

Rule 60(b)(3) 7, 8

Federal Rules of Evidence

Rule 703 ..... passim

Rule 901 4

Other Authorities:

2 M. H. Graham, *Handbook of Federal Evidence*, § 703.1, p. 105 & n.14 (4th ed. 1996) 1

TABLE OF AUTHORITIES (continued)

Page(s)

3 Mueller & Kirkpatrick, *Federal Evidence* § 357 (2d ed. 1994).....1

9 *Moore's Federal Practice Guide*, § 46.02[3] (3d ed. 2000).....6

Epps, *Clarifying the Meaning of Federal Rule of Evidence 703*, 36 B.C. L. Rev. 53 (1994).....1

Imwinkelried, *Developing a Coherent Theory of the Structure of Federal Rule of Evidence 703*, 47 Mercer L. Rev. 447 (1996).....1

REPLY BRIEF FOR PETITIONERS

Plaintiffs fail to address the question presented. The issue is not, as plaintiffs posit, "whether the court or the expert has the final word on what has been 'reasonably relied upon'" for purposes of admitting opinion testimony under the Federal Rules of Evidence. Opp. at 11. Rather, it is whether in evaluating a Rule 703 challenge to the unreliability of opinion testimony, district courts need to consider whether the underlying facts, data and information supporting the opinion are sufficiently trustworthy to make the expert's reliance on them reasonable in the particular case. Plaintiffs do not dispute that this question has broad practical implications in virtually every trial conducted in federal courts. Plaintiffs likewise concede that the circuits have split on this question.[1] Plaintiffs nevertheless claim that *Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579 (1993), has healed the split of authority in the circuits.

In fact, the conflict has not vanished. Contrary to plaintiffs' reading of the cases, post-*Daubert* decisions of both the Ninth and Sixth Circuits continue to follow the "liberal" approach to Rule 703. Plaintiffs do not dispute that the Second, Third, Fifth, Seventh, Tenth, and Eleventh Circuits apply the more rigorous "restrictive" approach. Hence, certiorari should be

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[1] *See, e.g., In re "Agent Orange" Product Liability Litigation*, 611 F. Supp. 1223, 1243-44 (E.D.N.Y. 1985), *aff'd*, 818 F.2d 187 (2d Cir. 1987). *See generally* 2 M. H. Graham, *Handbook of Federal Evidence*, § 703.1, p. 105 & n.14 (4th ed. 1996); 3 Mueller & Kirkpatrick, *Federal Evidence* § 357 (2d ed. 1994); Epps, *Clarifying the Meaning of Federal Rule of Evidence 703*, 36 B.C. L. Rev. 53 (1994); Imwinkelried, *Developing a Coherent Theory of the Structure of Federal Rule of Evidence 703*, 47 Mercer L. Rev. 447 (1996).

granted to permit this Court to resolve the conflict and adopt the restrictive approach to Rule 703, which requires district courts to evaluate the reasonableness and reliability of the data on which expert testimony is based.

Application of the proper standard here mandates reversal of the windfall judgment awarded to plaintiffs. Petitioners properly preserved the issue for review, and the mere fact that the loan documents underlying the expert's opinion were admitted in evidence does not dispose of petitioners' challenge to the testimony. Under Rule 703, the pertinent inquiry is not the admissibility of the data supporting the expert's opinion but their reliability. The assumptions of plaintiffs' expert as to the interest rates applicable to the BanRural loans were inconsistent with the bank's actual practices. This is confirmed not only by petitioners' post-trial submissions but also by the evidence admitted at trial. Hence, these underlying data lacked the requisite guarantees of trustworthiness to support admission of the opinion, and the district court's error in refusing to exclude it has produced a miscarriage of justice.

A. The Circuits Are in Conflict.

Notwithstanding *Daubert*, both the Ninth Circuit and the Sixth Circuit continue to follow the erroneous liberal approach to Rule 703. Plaintiffs do not dispute that the restrictive approach is proper and acknowledge that the pre-*Daubert* decisions of the Sixth Circuit are in the liberal camp.[2] Plaintiffs appear to suggest, however, that post-*Daubert*, there is no evidence that either the Sixth or the Ninth Circuit would apply the liberal approach. This suggestion is at odds with the recent reported decisions of both courts cited in the petition.

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[2] *E.g., Manniano v. Int'l Mfg.*, 650 F.2d 846, 853 (6th Cir. 1981).

In discussing the Sixth Circuit jurisprudence, plaintiffs conveniently ignore *Trepel v. Roadway Express*, 194 F.3d 708 (6th Cir. 1999), which was cited in the petition. Pet. at 10. Plaintiffs represent to the Court that "the pre-*Daubert* split will be completely healed once the Sixth Circuit has had an opportunity to address the question [presented for review in this case] with *Daubert* as guidance." Opp. at 10-11. Some six years after *Daubert*, however, the Sixth Circuit had such an opportunity in *Trepel*, but continued to adhere to the liberal view of Rule 703.

In *Trepel*, the plaintiff sued for damages based on a negligence theory after a valuable African woodcarving was broken in transport. Plaintiff's expert testified in part based on hearsay phone conversations plaintiff had with a woman who owned a similar carving and had said she had been offered $2.5 million for hers and would sell it only for $3 million. The Sixth Circuit invoked its prior decision in *Manniano* and held that the proffered opinion testimony was admissible because it was based on the type of information on which experts in the field customarily relied. 194 F.3d at 716-17. The dissenting opinion, however, would have required more: that the information be sufficiently trustworthy to make such reliance reasonable in the particular case. *Id.* at 719 (Suhrheinrich, J., dissenting in part). According to the dissent, the hearsay statements were unreliable and untrustworthy, which made it unreasonable for the expert to rely on these statements under Rule 703. *Id.* at 719-22. Thus, contrary to plaintiffs' analysis, *Daubert* has not affected the Sixth Circuit's approach to the issue presented for review in this case.

Likewise, plaintiffs distort the Ninth Circuit's jurisprudence. The Ninth Circuit has not adopted the restrictive approach and remains, along with the Sixth Circuit, in the liberal camp. The decision below speaks for itself: the Ninth Circuit approved of admission of the opinion testimony on the basis that "[i]t is common

sense that certified public accountants reasonably rely on loan agreements to calculate the interest due on loans." App. 8a. Thus, according to the Ninth Circuit, the district court below had no obligation to determine whether the expert's reliance on the loan agreements was reasonable under the circumstances of this case.[3]

Moreover, it is not the case, as plaintiffs claim, that the decision in *McKendall v. Crown Control Corp.*, 122 F.3d 803 (9th Cir. 1997), "indicates that the 'restrictive' approach has gained acceptance" in the Ninth Circuit. Opp. at 10. *McKendall* is not a Rule 703 case and does not even mention Rule 703. Thus, it is erroneous for plaintiffs to insinuate that the citation of *McKendall* in a dissenting opinion in *Sementilli v. Trinidad Corp.*, 155 F.3d 1130 (9th Cir. 1998), somehow can be equated with acceptance by the Ninth Circuit of one of the two competing Rule 703 standards.[4]

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[3] Plaintiffs place heavy reliance (*see* Opp. at 3, 6, 13-14) on the district court's statement that "in this instance, I have no difficulty feeling that these loan documents have some index of reliability for what they purport to be." App. 19a. It is difficult to understand how this observation by the trial judge affects the Rule 703 analysis. The court's statement appears to be related to the question of authenticity—a Rule 901 matter—rather than the reliability of the expert's interpretation of the loan documents as being consistent with BanRural's conduct. The latter, rather than the former, is the issue presented by the Rule 703 challenge to admission of the expert's opinion.

[4] In *Sementilli*, the Ninth Circuit reversed an order granting summary judgment based on the district court's refusal to consider opinion testimony proffered in opposition to the motion that the trial judge determined to be "pure speculation" and unreliable. 155 F.3d at 1133. The dissent in *Sementilli* (*id.* at 1141 (B. Fletcher, J., dissenting)) quoted a footnote in *McKendall* addressing the "conflicting pronouncements" regarding *Daubert* and its application to all expert testimony. *See McKendall*, 122 F.3d at 806 n.1. This citation, however, does not undermine petitioners' argument

(footnote continued)

In short, *Daubert* provides guidance but is not controlling. Unless this Court grants certiorari, the Ninth and Sixth Circuits will continue to be free to follow the erroneous liberal approach to admissibility under Rule 703.

B. The Rule 703 Analysis Does Not Turn on Whether the Underlying Facts, Data and Opinions Have Been Admitted.

Plaintiffs are correct that one of the purposes of Rule 703 is to liberalize common law practice and permit experts to rely on hearsay or otherwise inadmissible sources, provided guarantees of trustworthiness and reliability are maintained. Rule 703 is not by its terms, however, limited to consideration of the types of inadmissible matters that may support an otherwise admissible expert opinion. Moreover, the simplistic paradigm that plaintiffs seek to construct—that Rule 703 has no application if the expert claims to rely for an opinion on matters that have been admitted in evidence—turns the law on its head: reliability, not technical admission of evidence, remains the foundation of Rule 703 analysis.

The fact that certain materials have been admitted into evidence does not insulate them from the rigors of Rule 703. *See Bauman v. Centex Corp.*, 611 F.2d 1115, 1120 (5th Cir. 1980) ("In general whether facts relied on by an expert are in evidence, or even could be in evidence, is not relevant. The pertinent inquiry under Rule 703 is whether the facts are of a type reasonably relied on by experts in the particular field. The object of this inquiry is of course to determine the reliability of the expert's testimony."). The question whether

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that the restrictive approach has only been espoused in dissenting opinions in the Ninth Circuit, much less does it support plaintiffs' claim that the Ninth Circuit is no longer in Rule 703's liberal camp.

evidence has been "reasonably relied upon" requires a judge to determine whether the evidence relied on is the type customarily relied on and then whether those materials are reliable in fact. The admission of the underlying data is relevant to this inquiry. It is not a substitute, however, for the exercise of the district court's gatekeeping function through application of the restrictive approach to assess the reliability of the proffered opinion testimony under Rule 703.

C. Petitioners Have Preserved the Issue for Review.

The Ninth Circuit had adequate opportunity to consider and decide the legal issue as to which petitioners seek review in this Court. Petitioners briefed and argued the issue of the lack of reliability of the foundation for the expert opinion in the Ninth Circuit. *See* App. at 7a-8a. That suffices to preserve the issue: petitioners are not required to brief the circuit conflict below to preserve the issue for certiorari.

Moreover, in any event, the issue was again briefed, with citation to *Daubert,* in petitioners' petition for rehearing. Pet. for Reh. at 5 & n.2. Raising an issue in a petition for rehearing preserves the issue for further appellate review. *See Richards v. Jefferson County*, 517 U.S. 793, 797 n.3 (1996) ("Because petitioners raised their due process challenge to the application of res judicata in their application for rehearing to the Alabama Supreme Court, that federal issue has been preserved for our review.").

Likewise, the reliability of the evidence relied on by plaintiffs' expert was properly objected to at trial. Federal Rule of Civil Procedure 46 requires only that the court be put "on notice." *See* 9 *Moore's Federal Practice Guide*, § 46.02[3] (3d ed. 2000). "The Supreme Court has ruled that a plaintiff preserves his objection if counsel puts the trial court on notice as to his concerns, even though counsel might have been more articulate when stating the grounds for objection."

Id. Counsel for petitioners drew the trial court's attention to the unreliability of the evidence used as the basis for the expert's opinion. App. 17a.

Thus, petitioners timely challenged the erroneous, unfounded and highly prejudicial opinion testimony at every stage of this case. Plaintiffs' arguments to the contrary are mere wishful thinking.

D. Plaintiffs Misstate the Record.

Plaintiffs attempt to persuade this Court that it should not be disturbed by the grievous error upon which the judgment below rests and the resulting $6 million windfall. However, plaintiffs' efforts in this regard are based on a pervasive misrepresentation of the record. Most disturbing are plaintiffs' claims that the evidentiary basis for challenge to the erroneous expert opinion did not exist until after the trial (*see* Opp. at 2-5, 7) and that the $12.5 million judgment represented a "compromise verdict." *See* Opp. at 1-2.

The inadmissibility of the expert's testimony does not depend on the showing made in petitioners' post-judgment motion under Rule 60(b)(3). As explained in the petition, the trial record itself reflects the dramatic inconsistency between BanRural's actual practices in assessing loan interest and plaintiffs' expert's skewed assumptions as to what the bank supposedly was doing. *See* Pet. at 5. Plaintiffs offer no satisfactory explanation for this transparent conflict.[5]

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[5] In a footnote, plaintiffs attempt to deal with this through obfuscation. First, according to plaintiffs, "the interest rate the bank utilized in the period immediately *before* the peso's slide accelerated in early 1995, differs from the rate the accountant used for the time periods *after* the peso plummeted." Opp. at 3-4 n.5 (original emphasis). The problem is that the record below is uncontradicted that the devaluation of the peso occurred in late December 1994 (RT 1702) and devaluation cannot in any event explain why plaintiffs' expert concluded that the bank would have charged

(footnote continued)

In any event, plaintiffs' attempt to debase the evidence offered in support of petitioners' Rule 60(b)(3) motion is groundless. Plaintiffs represent to this Court that petitioners' evidence was mere "hearsay . . . indicating that the Mexican bank might be willing to apply a lower interest rate" and that "[a]lthough they had the opportunity to do so, [petitioners] declined . . . to authenticate the evidence they had regarding the Mexican bank's position." Opp. at 3.

None of this is true. Petitioners propounded post-trial letters rogatory to the bank (ER 381) and presented BanRural's response to the letters in support of the Rule 60(b)(3) motion. ER 416, 483. Petitioners also submitted an affidavit by the responsible bank officer attesting that, as of six months after trial, the amount of the debt was less than $5.5 million. ER 1242-46. Thus, the Rule 60(b)(3) showing, which was uncontroverted on this point, left no doubt as to the actual amount due on the bank's loans.

Plaintiffs try to avoid the implication of this evidence by claiming that the jury's catastrophic $12.5 million award was simply a "compromise verdict." This too is false. It is true that plaintiffs originally claimed damages totaling in excess of $25 million. By the end of trial, however, plaintiffs had

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interest at an annual rate in excess of 90% on April 8, 1995 when the bank's own records reflected that on April 7 interest was accruing on the loans at rates ranging from 13.5% to 23.7%.

Next, plaintiffs urge that their accountant checked his calculations and testified that they were consistent with BanRural's own calculations. Opp. at 3-4 n.5. If, as he testified, however, the accountant "checked" his "methodology" with the bank statements, such a check would have revealed that his interest assumptions were inaccurate, and the drop in the exchange rate for the Mexican peso cannot explain the discrepancy.

reduced their demand and requested in closing argument that the jury award them $15.7 million. Of that amount, $11.4 million supposedly represented plaintiffs' alleged liability to BanRural, and $4.3 million reflected lost profits and other damages. RT 3275-79. Thus, despite all of plaintiffs' denials, the jury's $12,516,000 verdict against petitioners (App. 14a-15a.) necessarily was based on their expert's testimony concerning the BanRural loans.

For these reasons, the record leaves no doubt that the award represents a $6 million windfall to plaintiffs. Accordingly, certiorari should be granted so that this Court may resolve the split of authority and, in so doing, debunk the liberal approach to Rule 703 that produced this irrational and unconscionable result.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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